Fordham International Arbitration Conference

Facing the Future in International Arbitration: Evolving Issues, Practices and Solutions

Friday, November 17, 2017 | 9 a.m. – 5:45 p.m.

CLE Materials & Speaker Biographies
Fordham Law School, 150 West 62nd Street, New York City
Facing the Future in International Arbitration: Evolving Issues, Practices and Solutions

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Moselle, Dr. Boaz & Gibson, Colm. The role of the expert in price review arbitrations. Global Law and Business.


Sussman, Edna. Improving your Arbitration Presentation with the Mock Arbitration: Two Case Studies, New York Dispute Resolution Lawyer, Fall 2012 vol. 5, No. 2.

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**Speakers Biographies**

**Mohamed S. Abdel Wahab**  
Professor of Law, Cairo University; Arbitrator, Zulficar & Partners Law Firm

Mohab holds the following positions: chair of private international law and professor of dispute resolution at Cairo University; founding partner and head of international arbitration at Zulficar & Partners Law Firm; vice president of the ICC International Court of Arbitration; court member of the LCIA; president of LCIA’s Arab Users’ Council; court member of the CIAMC, vice chair of the IBA Arbitration Committee; member of the CIARB’s Practice and Standards Committee; member of the CRCICA Advisory Committee; member of AAA-ICDR International Advisory Committee; and member of the SIAC African Users’ Council Committee. He has served as arbitrator, counsel, or legal expert in more than 175 cases involving parties from the Middle East, Europe, Asia, Canada, and the United States. He has appeared in cases under the auspices of the AAA-BCDR, CRCICA, DIAC, DIICLCIA, ICC, ICSID, LCIA, LMMA, SCC, SIAC, as well as ad hoc UNCITRAL proceedings and governed by Bahraini, Egyptian, English, French, Jordanian, Kuwaiti, Libyan, New York, Omani, Pakistani, Qatari, Saudi, Singaporean, Spanish, Swiss, Syrian, Italian and United Arab Emirates law(s), as well as the general principles of law.

Wahab is included in Who’s Who Legal: Arbitration, the GAR Global Guide for Future Leaders in International Arbitration (2017), and the GAR Guide on Thought Leaders in International Arbitration (2017)—among only 33 world-class practitioners worldwide. Who’s Who Legal (2017-2018) has said that Mohamed Abdel Wahab is “one of the best practitioners in the world today” thanks to his “sharp mind and excellent legal knowledge.”

**Philip K. Anthony**  
Chief Executive Officer, DecisionQuest, Inc.

Anthony is chief executive officer of DecisionQuest, Inc., a trial consulting and strategic communications firm with offices in Los Angeles, Chicago, Pennsylvania, New York, Boston, Washington DC, Atlanta, San Francisco, Miami, and Minneapolis. Anthony is an adjunct professor at the University of California Irvine Law School and a board member of the University of Southern California and a trustee of the University of California Irvine.

With a career spanning over 30 years, Anthony has built a reputation as one of the nation’s leading and most sought-after trial consultants. He has shared his vast expertise as a frequent lecturer at the American College of Trial Lawyers, the American Bar Association (ABA), the Association of Business Trial Lawyers (ABTL), Practicing Law Institute, and the National Institute for Trial Advocacy (NITA). He is an author and contributor to six books and numerous articles on the nuances of trial strategy.

With a Ph.D. in psychology, communications, and business from University of Southern California, Anthony has offered unique legal insights on CBS News, NBC News, and National Public Radio, and has been quoted in such prestigious publications as The Wall Street Journal, The Los Angeles Times, The New York Times, Time Magazine, among others.

**R. Doak Bishop**  
Partner, King & Spalding

Bishop is partner in King & Spalding’s Houston office and co-chair of the firm’s international arbitration practice group. He has a B.A. with high honors and departmental distinction from Southern Methodist University (1973), and J.D. degree with honors from the University of Texas Law School (1976), where he was research editor of the Texas Law Review. He has 40 years of legal practice, with a focus on international arbitration and foreign investment disputes. He is board certified in civil trial law by the Texas Board of Legal Specialization. He is on the executive committee of the American Society of International Law, the board of trustees of the Center for American and International Law. He has served as chair of the Institute of Transnational Arbitration (2012-2015) and a member of the U.S. delegation to the NAFTA Advisory Committee on Private Commercial Disputes. He is advisor to the American Law Institute's Restatement of the Law (3rd) of International Commercial Arbitration, and has been an adjunct professor at the following institutions: SMU Law School (1999) (International Commercial Arbitration), University of Houston Law School (2002) (Foreign Investment Disputes), University of Texas Law School (2014) (Foreign Investment Disputes), and University of Oklahoma Law School (2012, 2013, 2015) (Foreign Investment Disputes). He has served as co-chair of the international litigation committee of ABA’s Litigation Section (1998-2000) and chair of the Litigation Section of the State Bar of Texas (1998-1999). He has served as arbitrator in about 80 arbitrations, including ICSID, LCIA, ICC, AAA/ICDR, NAFTA, and BIT arbitrations. He is editor of The Art of Advocacy in International Arbitration (2nd ed. Juris Publishing 2010), co-author of Foreign Investment Disputes: Cases, Materials and Commentaries (Kluwer, 2nd ed. 2014), editor of Enforcement of Arbitral Awards Against Sovereigns (Juris 2009), and co-author of Annulment Under the ICSID Convention (Oxford Press 2012).

**Christopher Bogart**  
Chief Executive Officer, Burford Capital

Bogart co-founded Burford Capital and is the chief executive officer. After working at Cravath Swaine & Moore as a litigator, Bogart moved to Time Warner where, as executive vice president & general counsel of Time Warner Inc., he managed one of the largest legal functions in the world, with more than 350 lawyers. He also served as chief executive officer of Time Warner Cable Ventures and as chief executive officer of Time Warner Entertainment Ventures. Bogart was the gold medalist and graduated with distinction from the Faculty of Law of the University of Western Ontario, and served as a law clerk to the chief justice of Ontario.

**The Honorable Charles N. Brower**  
International Judge and Arbitrator; Judge, Iran-United States Claims Tribunal; Judge ad hoc, International Court of Justice; Member, 20 Essex Street Chambers

Judge Brower has been an international judge for 34 years, including serving as judge ad hoc on the Inter-American Court of Human Rights. His public service includes four years in the Office of the Legal Adviser of the Department of State, including as the acting legal adviser, and a period in the White House as deputy special counsellor to the president of the United States (sub-Cabinet rank as deputy assistant to the president). His many appointments as international arbitrator caused The American Lawyer recently to dub him “the reigning king of international arbitrators.” Interspersed with decades of public service he was for many years a partner of White & Case LLP in New York and Washington, D.C. Judge Brower holds a B.A. (cum laude) from Harvard College, a J.D. from the Harvard Law School, and was a Fulbright scholar in Germany.

**Andrea Carlevaris**  
Partner, BonelliErede

Carlevaris is a partner at BonelliErede. He is based in Paris and Milan.

Between September 2012 and May 2017, Carlevaris has been the secretary general of the ICC International Court of Arbitration and the director of the ICC Dispute Resolution Services. Before joining the ICC Court, he was a partner in the Rome office of Bonelli Erede Pappalardo, which he joined in 2003. He was also a member of the ICC International Court of Arbitration and of the ICC Commission on Arbitration. He has acted as an advocate or as an arbitrator in numerous proceedings (ICC, ICSID, UNCITRAL, Milan Chamber of Arbitration).

Carlevaris is currently a member of the board of directors of EFILA (the European Forum of International Law and Investment), IMI (International Mediation Institute) and AIA (the Italian Association for Arbitration), a founding member and member of the advisory board of Arbit (the Italian Forum for International Arbitration and ADR) and a member of the steering committee of the...
Stephanie Cohen
Independent Arbitrator

Cohen is a Canadian arbitrator based in New York City. She frequently sits as tribunal chair or sole arbitrator in international commercial disputes, and is also among the first 30 emergency arbitrators appointed by the ICC. Cohen has heard cases under the ICC, ICDR, AAA, SMA, and UNCITRAL rules and is a member of the international and domestic arbitration panels for the AAA/ICDR as well as a fellow of the Chartered Institute of Arbitrators. Previously, Cohen was counsel in the international arbitration and commercial litigation practice groups at White & Case LLP in New York where she represented clients in complex, high-value disputes before international arbitration tribunals and courts. She is a graduate of McGill University and the University of Toronto Faculty of Law and is dually qualified as a lawyer in New York and Ontario, Canada. Who’s Who Legal (2018) recognizes Cohen as one of the “most highly regarded” arbitration practitioners aged 45 or under and says she is “an entrepreneurial and courageous independent arbitrator who excels in international commercial disputes.” (www.cohenarbitration.com)

Franco Ferrari
Professor of Law; Director, Center for Transnational Litigation, Arbitration and Commercial Law; NYU School of Law

Ferrari was most recently a chaired professor of international law at Verona University in Italy (2002-2016). Previously, he was a chaired professor of comparative law at Tilburg University in the Netherlands (1995-1998) and the University of Bologna in Italy (1998-2002). After serving as a member of the Italian delegation to various sessions of the United Nations Commission on International Trade Law (UNCITRAL) from 1995 to 2000, he was legal officer at the United Nations Office of Legal Affairs, International Trade Law Branch, from 2000 to 2002, where he was responsible for numerous projects, including the preparation of the UNCITRAL digest on applications of the UN Sales Convention. Ferrari has published more than 280 law review articles in various languages and 20 books in the areas of international commercial law, conflict of laws, comparative law, and international commercial arbitration. Ferrari is a member of the editorial boards of various peer-reviewed European law journals (Internationales Handelsrecht, European Review of Private Law, Contratto e impresa, Contratto e impresa/Europa, and Revue de droit des affaires internationales). Ferrari received his LL.M. from Augsburg University, Germany and J.D. from Bologna University, Italy.

Susan Franck
Professor, American University, Washington College of Law

Franck is a world-renowned expert in international arbitration and economic law. Her scholarship involves writing over 40 publications and making more than 120 presentations, which have led to her being cited in reports from the U.S. Department of State and American Bar Association, as well as being quoted in the popular press including in the Wall Street Journal. She has provided expert commentary to the United Nations Conference on Trade and Development, International Centre for the Settlement of Investment Disputes, Inter-American Development Bank, Asian-Pacific Economic Cooperation, and developed and developing states. Franck is the chair of the academic council of the Institute for Transnational Arbitration, an elected member of the American Law Institute, and a member of the Executive Council of the American Society of International Law. She received her B.A. in psychology and political science from Macalester College, her J.D. from the University of Minnesota, and obtained her LL.M. at Queen Mary’s University of London after winning a U.S.-U.K. Fulbright Grant to study international dispute resolution. Franck is qualified to practice law in England and Wales, Minnesota, and the District of Columbia.

Clayton P. Gillette
Max E. Greenberg Professor of Contract Law, NYU School of Law

Gillette teaches in the areas of commercial law, contracts, and local government law. He is the author, with Steven D. Walt, of The UN Convention on Contracts for the International Sale of Goods: Theory and Practice (Cambridge University Press 2016), Advanced Introduction to International Sales Law (Elgar 2016); and Sales Law: Domestic and International (3d ed. Foundation 2016). He has written numerous articles on various aspects of commercial law, including long-term contracts, damages, the law and economics of contract law, and commercial opportunism. Gillette's work explores subjects ranging from the appropriate degree of municipal fiscal autonomy, to the role of reputation in commercial transactions, to the political economy of international sales law. Gillette received his B.A. from Amherst College and his J.D. from the University of Michigan School of Law. Prior to joining the NYU faculty, Gillette served as the Perre Bowen Professor of law at the University of Virginia School of Law, and as professor of law and Warren Scholar in Municipal Law at Boston University. He was vice dean at NYU School of Law from 2004 to 2007. Before entering academia, Gillette clerked for Judge J. Edward Lumbard of the United States Court of Appeals for the Second Circuit, and was
Teresa Giovannini
Founding Partner, LALIVE

Giovannini is a founding partner of LALIVE (1994) specializing in international arbitration (including setting aside proceedings with the Swiss Supreme Court), as well as art law. She has acted in more than 180 international arbitrations (among which 120 as arbitrator, including 84 as presiding or sole arbitrator), either ad hoc or administered by various institutions (AAA/ICDR, ICC, ICHEIC, ICSID, LCIA, etc.). Giovannini is the Swiss member of the ICC Court of Arbitration and the ICC Commission on Arbitration and ADR since 1 July 2015, after having been a member and vice-president of the LCIA Court from 2006 until 2011 and a member of the Arbitral Council of the Milan Chamber of Arbitration from 1997 to 2005. She is also part of several panels of arbitrators (ICC Swiss National Committee, ICDR, LCIA, etc.) as well as of arbitration committees (board of directors of the American Arbitration Association, ICC Institute Council, global advisory board of the New York International Arbitration Centre, LCIA Company, Club of Arbitrators of the Milan Chamber of National and International Arbitration, etc.). Giovannini is a frequent speaker and lecturer on international arbitration and the author of various publications in the field. She has been ranked by Chambers, Legal Experts Europe, the International Who’s Who of Commercial Arbitration, and the Global Arbitration Review for many years.

Louis B. Kimmelman
Partner and Co-Leader, Global International Arbitration Practice, Sidley Austin LLP, New York Office

Kimmelman focuses on the arbitration and litigation of complex commercial and investment treaty disputes as well as litigation in aid of the arbitration process. Kimmelman regularly represents U.S. and foreign clients, as well as sovereign entities, in international disputes before arbitral tribunals and state and federal courts in the United States. He has acted as lead counsel and as arbitrator in numerous cases before the leading international arbitration institutions. He is an adjunct professor of law at Brooklyn Law School and Georgetown University Law Center, where he teaches International Commercial Arbitration, as well as an adviser to the American Law Institute project on the Restatement of the U.S. Law of International Commercial Arbitration. He received his B.A. degrees from Yale University and his and J.D. degree from Yale Law School.

James Lawrence
Executive Director, Blakely Advocacy Institute, University of Houston Law Center

Lawrence serves as the executive director of the Blakely Advocacy Institute at the University of Houston Law Center. The Blakely Institute provides skills training to over 400 law center students each year. He also directs the law center’s highly successful Moot Court Interscholastic Competition Program and Alternative Dispute Resolution Interscholastic Competition Program. Over the past five years, both programs have fielded intercollegiate teams that have won over 38 international, national, and regional titles.

He specializes in the alternative dispute resolution process, with a focus on legal negotiation and communication. He designed and teaches several of the law center’s Alternative Dispute Resolution courses including Legal Negotiations, Advocacy Survey, and Advanced Negotiations. He has taught Negotiations in the University of Houston, Bauer College of Business Executive M.B.A. program and he also serves on the Professional Sports Counseling Panel for the University of Houston Athletic Department, where he works with University of Houston athletes, on an as needed basis, in their negotiations with professional agents.

Lawrence is a principal with Trial Science Solutions, a national and international trial and arbitration advocacy consulting firm where he engages in the study of judge, jury, and arbitration decision making and the development of successful trial and arbitration advocacy. He is the communications expert for the American Bar Association/National Institute for Trial Advocacy’s Family Law Trial Advocacy Institute and he has served as a program director and faculty member for many other courses offered by NITA.

He is a fellow in the Chartered Institute of Arbitrators and is vice chair for Membership of the North American Branch of CIARB. He is certified to teach the Member Level Course for the Chartered Institute and he is currently a co-editor for the American Arbitration Association’s Yearbook on Arbitration and the Law. He holds a certificate in advanced arbitration skills from the law center’s A.A. White Dispute Resolution Center and he is a qualified mediator in Texas. Lawrence is a featured speaker in advocacy training programs both nationally and internationally.

M. Alexis Maniatis
President and CEO, The Brattle Group, Inc

Maniatis has more than 25 years of experience providing consulting and expert witness testimony and advising clients on valuation and damages issues in expropriations, contract disputes, competition-related litigation, asset and merger transactions, and regulatory proceedings. He has addressed issues including development of expected cash flows, discount rates, control premia, country risk adjustments, preemption interest, and interpretation of acquisition transactions and publicly traded company values. Maniatis is recognized as one of the world’s arbitration expert witnesses by Global Arbitration Global Arbitration Review’s The International Who’s Who of Commercial Arbitration. He hold a bachelor’s degree in economics from Wesleyan University and an M.B.A. from Yale University.

Michael McIlwrath
Executive Counsel, Litigation, GE

McIlwrath is a graduate of UC Berkeley and Cornell Law School. He practiced in the litigation department of Willkie Farr & Gallagher in New York City, and joined GE in 1999 in Florence, Italy, as the global lead litigation counsel for GE Oil & Gas, a world leading supplier of technology in the oil and gas industry (as of July 2017 part of Baker Hughes, a GE Company).

He is co-author of International Arbitration and Mediation: A Practical Guide (Kluwer Law International 2010), a regular contributor to the Kluwer Arbitration Blog, and was the chair of the Global Pound Conference in 2016-17. McIlwrath is a member of the governing body for dispute resolution of the International Chamber of Commerce (ICC), the board of directors and past chairman of the International Mediation Institute (IMImediation.org), the advisory boards of the Singapore International Arbitration Centre, the Vienna International Arbitration Centre, and Arbitrator Intelligence. He was recently recognized by Arbitral Women as the organization’s Champion of Change in 2017 for promoting diversity in international arbitration.

Ina C. Popova
Partner, Debevoise & Plimpton

Popova is a partner in Debevoise & Plimpton’s international dispute resolution group who focuses on international arbitration and litigation and public international law. Popova is admitted to practice in Paris and New York and holds advanced degrees in English law. Fluent in several languages, Popova leads matters in French and Spanish and regularly handles disputes arising out of Africa and Latin America. She has particular expertise in matters in the mining, energy, and technology, media and telecommunications sectors. She sits as arbitrator and serves as counsel in a broad range of international matters.

Popova is recognized within the legal community as one of the top international lawyers of her generation. She is listed in Who’s Who Legal Arbitration (main edition), was named...
one of the top 40 up-and-coming lawyers nationwide by the American Bar Association, is recognized a “Future Star” and member of the “Under 40 Hot List” by Benchmark Litigation, and is one of only six international arbitration Next Generation Lawyers by Legal 500. Who’s Who Legal Arbitration – Future Leaders describes Popova as “very bright, impressively efficient and extremely well liked in the community.”

Popova serves in a number of leadership positions, including on the Court of the Casablanca International Mediation and Arbitration Center (CIMAC), on the 2018 ICCA Program Committee, as past co-chair of the annual meeting of the American Society of International Law, advisory board member of the Institute for Energy Law, and rapporteur for the ASIL-ICCA Joint Task Force on Issue Conflicts in Investor-State Arbitration. She has taught law at the Institut d’Études Politiques de Paris (Sciences Po) and is a fellow of the Société de Législation Comparée. She speaks and writes regularly on arbitration-related issues.

William W. Park
Professor of Law, Boston University

Park teaches at Boston University in the areas of international tax and finance. After studies at Yale and Columbia, he practiced in Paris until returning home to Boston, where he served as director of Boston University’s Center for Banking Law.


Jonathan Putnam
Founder and Principal, Competition Dynamics

Putnam is an expert in intellectual property, antitrust, and technological change. Putnam regularly testifies in large-scale intellectual property litigation, in federal, state, and bankruptcy courts, before the Federal Trade Commission and International Trade Commission, and in U.S. and international arbitrations.

Before founding Competition Dynamics, Putnam held a chair in the law and economics of intellectual property at the University of Toronto. He has also held academic appointments at Vassar College, Columbia University, Yale University, and Boston University. He is the editor of Intellectual Property Rights and Innovation in the Knowledge-Based Economy (2006). His Ph.D. dissertation was the first to measure the global value of patent rights.

Catherine A. Rogers
Professor of Law, Penn State Law and Queen Mary

Rogers teaches at Penn State Law and is an affiliate faculty member of the School of International Affairs; she has a dual appointment as professor of ethics, regulation, and the rule of law at Queen Mary, University of London, where she is also co-director of the Institute of Regulation & Ethics. Rogers is a reporter for the American Law Institute’s Restatement of the U.S. Law (Third) of International Commercial Arbitration, a member of the board of directors of the Lagos Court of Arbitration, a member of the international advisory board of the Vienna International Arbitration Center, and co-chair, together with William W. “Rusty” Park and Stavros Brekoulakis, of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration. She is the founder of Arbitrator Intelligence, a nonprofit organization that aims to increase transparency, accountability and diversity in the arbitrator selection. Rogers’ scholarship focuses on the convergence of the public and private in international adjudication, the intersection of markets and regulation in guiding professional conduct, and on the reconceptualization of the attorney as a global actor. Rogers regularly engages in arbitration-related capacity-building efforts around the world. Her book, Ethics in International Arbitration, was published by Oxford University Press in 2014.

Claudia T. Salomon
Partner, Latham & Watkins

Salomon is a partner in the New York office of Latham & Watkins and global co-chair of the firm’s international arbitration practice. She is recognized as a leading international arbitration attorney by Chambers USA, The Legal 500, Who’s Who Legal, Latinvex, and Best Lawyers.

She has experience handling significant investor treaty arbitration and international commercial arbitration cases under all of the major arbitral rules, in venues around the globe, under common law and civil law. She also regularly serves as an arbitrator.

Salomon is the U.S. member of the ICC International Court of Arbitration and serves as the co-chair of the ICC Taskforce on Financial Institutions and International Arbitration. She is the co-editor of Choice of Venue in International Arbitration, published by Oxford University Press. She is admitted to practice in New York and England & Wales and is a graduate of Harvard Law School.

Pablo T. Spiller
J. Jacobs Distinguished Professor of Business & Technology, University of California, Berkeley and Compass Lexecon

Spiller, Ph.D. economics, University of Chicago, is a senior consultant at Compass Lexecon. He is also the Jeffrey A. Jacobs Distinguished Professor Emeritus of Business and Technology at the Haas School of Business, University of California, Berkeley; research associate at the National Bureau of Economic Research; and the former president of the International Society for New Institutional Economics and an elected member of the board of directors of the American Law & Economics Association.

Spiller has written extensively on regulatory, antitrust, and institutional issues, having published more than 130 academic articles and 10 books. Spiller has also extensive consulting and expert testimony experience, having testified in more than 130 litigation and international arbitration cases, involving both treaty and contractual disputes rendering opinions on damages, contract interpretation and regulatory issues in a variety of sectors throughout the world. He has testified in jurisdictions such as the ICSID, ICC, LCIA, and AAA. He has also consulted extensively with the World Bank, United Nations, and the Inter-American Development Bank as well as governments and private companies.

Spiller was the editor-in-chief and associate editor of the Journal of Law, Economics, and Organization for 19 years, and held multiple editorial appointments at a variety of academic journals. He was also the chair of the business and public policy group at the University of California, Berkeley for five years, and, on leave from Berkeley, served as special advisor to the director at the Bureau of Economics of the U.S. Federal Trade Commission.

Maya Steinitz
Professor of Law and Bouma Family Fellow in Law, University of Iowa College of Law

Steinitz teaches civil procedure, international business transactions, and international arbitration at the University of Iowa College of Law. In the Spring of 2018 she will teach a course on litigation and law firm finance and the future of the legal profession as a visiting professor at Harvard Law School. She has published extensively on litigation finance and has served as a consultant and expert witness on litigation finance and also serves as an international arbitrator. Prior to joining the University of Iowa College of

Edna Sussman
Independent Arbitrator and Mediator; Distinguished ADR Practitioner in Residence, Fordham Law School
Formerly a partner in the firm of White & Case LLP, Sussman has extensive experience having served as an arbitrator (as chair, sole, or co-arbitrator) in over 200 cases and as a mediator in over 200 cases in a wide variety of complex international and domestic commercial disputes under many institutional rules and ad hoc. She serves on many institutional panels around the world.

Sussman serves as chair of the AAA-ICDR Foundation, on the board of the American Arbitration Association, as vice-chair of the New York International Arbitration Center and is the co-chair of the annual Fordham International Arbitration Conference. She served as the president of the College of Commercial Arbitrators, as chair of the Arbitration Committees of the ABA's Dispute Resolution and International Sections, chair of the Dispute Resolution Section of the New York State Bar Association, chair of the ADR Committee of the Energy Bar Association and chair of the New York City Bar Association Energy Committee. Ranked annually for arbitration and mediation by Chambers USA and Chambers Global, Who's Who, Best Lawyers and SuperLawyers, Sussman has lectured and published widely on arbitration and mediation topics. www.sussmanadr.com

John M. Townsend
Partner and Co-Chair, Arbitration Practice, Hughes Hubbard & Reed LLP, Washington, DC
Townsend’s practice focuses on international disputes, including commercial and investment treaty arbitration; he is currently lead counsel in five investment treaty arbitrations against the Russian Federation involving its treatment of Ukrainian investors after its annexation of Crimea. Townsend is a former chairman of the board of directors of the American Arbitration Association and currently chairs the AAA’s Law Committee. president George W. Bush appointed him to be one of the American members of the panel of arbitrators of ICSID. He was the first chair of the Mediation Committee of the International Bar Association and is currently a vice-president of the Court of Arbitration of the LCIA and a member of the College of Commercial Arbitrators. Townsend received a B.A. in history from Yale University in 1968 and a J.D. from Yale Law School in 1971.

Eduardo Zuleta
Founder, Zuleta Abogados; Vice President, ICC International Court of Arbitration
Zuleta has acted as counsel, chair, co-arbitrator, and sole arbitrator in multiple arbitrations under international rules including ICC, ICDR, IACAC and UNCITRAL. He has been member of the ICSID panel (chairman’s list) and has acted in investment arbitrations under ICSID, UNCITRAL, and ICC and in annulment committees under ICSID.

Zuleta has a J.D. from El Rosario Law School in Colombia and has completed post graduate studies and a specialization from the University of London, Queen Mary. He has written extensively on arbitration and was recently appointed an adjunct professor at Georgetown.
AWARDS OF INTEREST IN INTERNATIONAL COMMERCIAL ARBITRATION:
NEW YORK LAW AND PRACTICE

COMMITTEE ON INTERNATIONAL COMMERCIAL DISPUTES

June 21, 2017
Interest on damages awarded by an arbitral tribunal can be a significant component of a prevailing party’s total recovery in international commercial arbitration. Uncertainty exists, however, with respect to the criteria that international arbitrators should apply in determining pre-award and post-award interest. One question that arises in domestic and international arbitrations governed by New York substantive law and seated in New York is whether the prejudgment interest provisions contained in Sections 5001, 5002 and 5004 of the New York Civil Practice Law and Rules (“N.Y.C.P.L.R.” or “C.P.L.R.”) apply to the determination of pre-award or post-award interest. The answer to the question whether arbitrators are obligated to (or should) apply New York’s nine percent statutory prejudgment interest rate can have a substantial economic impact on the parties in an arbitration.

Part I of this report sets forth an executive summary.

Part II provides a discussion of the standards applicable to interest determinations in international commercial arbitrations, with a focus on arbitrations that are both governed by New York substantive law and seated in New York. ¹

Appendix A sets forth summaries of pre-award and post-award interest determinations of arbitral tribunals in approximately 45 international commercial arbitrations governed by New York substantive law.


This report proposes a step-by-step approach that international arbitrators may apply to the determination of interest in international commercial arbitrations generally, and not merely in international commercial arbitrations governed by New York substantive law and seated in New York. This report does not address, however, the choice of law issues that may arise when the arbitral law of the seat of arbitration may conflict on the question of interest with the substantive law governing the dispute because no such conflict exists between New York arbitral law and New York substantive law. The report addresses the law of the seat of arbitration principally as a factor that arbitrators may wish to consider as one indication of party intent.
I. Executive Summary

International arbitrators have discretion to apply or not to apply New York’s statutory prejudgment interest provisions to the determination of pre-award and post-award interest in an international commercial arbitration governed by New York substantive law and seated in New York, in the Committee’s view, for several reasons. First, the text of C.P.L.R. Sections 5001 and 5002 contains numerous terms (including references to “the court’s discretion,” “the cause of action,” “the jury,” and “the clerk of the court”) indicating that these sections are intended to apply only to court proceedings, not arbitration. Second, the legislative history of C.P.L.R. Section 5004, which sets the prejudgment interest rate applicable under Sections 5001 and 5002, indicates that the New York State Legislature (the “NY Legislature”) adopted a fixed rate of nine percent in part in consideration of factors that are not directly related to the compensatory purpose of an award of interest and that arbitrators may or may not deem relevant to the award of interest in international arbitration. In particular, the NY Legislature’s adoption of a fixed rate in 1972 reflected its desire to simplify the calculation of interest by the courts; in 1981, after market rates of interest had risen into the high teens, the NY Legislature increased the fixed rate from six to nine percent in part to discourage defendants from using delay tactics in court proceedings. Third, although New York’s highest court has not had occasion to address squarely the applicability, or not, of New York’s prejudgment interest provisions to international or domestic arbitration, the State’s Appellate Divisions have held that these provisions do not necessarily...
apply to arbitrations and that an arbitral tribunal’s decision on this question is not subject to 
review by the courts.  

New York courts acknowledge that, in the absence of express party agreement on the 
interest rate to be applied, arbitrators have discretion to determine interest based on a broad range 
of considerations. It may be appropriate for an arbitral tribunal to determine pre-award and post-
award interest in accordance with New York’s prejudgment interest provisions if, by way of 
example only: evidence exists that the parties intended for the statutory prejudgment interest rate 
to apply, or no case is made in favor of applying a different rate, or the choice of interest rate 
would not have a significant economic impact one way or another. Arbitrators also have 
discretion to take into consideration that, as already noted, the NY Legislature adopted a fixed 
rate in part for the administrative convenience of the courts. Moreover, arbitrators may choose 
to consider to what extent New York’s nine percent rate differs from market rates prevailing 
during the pre-award period and/or economic factors specific to the parties such as their cost of 
funds. However arbitrators may choose to exercise their discretion to determine interest, in order 
to facilitate international enforcement the Committee recommends that the tribunal set forth 
clearly in its award the basis for its interest determination.

In the Committee’s view, thoughtful consideration of two guiding principles common to 
New York law and to international arbitration – the freedom of contracting parties to agree on 
the terms of their relationship, and the compensatory purpose of interest – should guide 
arbitrators in prioritizing the many factors that they may consider in awarding interest in a 
particular case. Generally, the more clearly a factor reflects the intent of the parties, the higher 
the priority an arbitral tribunal should give to that factor. A focus on party intent generally leads

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to an examination of key factors in the following order: (a) contractual stipulations on interest rates to be applied to one or more aspects of the contract; (b) guidance that may be found in the arbitration rules chosen by the parties regarding the award of interest; (c) the substantive law governing the merits of the case; and (d) the arbitration law of the seat of the arbitration. An arbitral tribunal should consider these indicators of party intent in light of the underlying compensatory purpose of interest awards subject to narrow exceptions based on public policy.

An arbitral tribunal engaged in the reasonable exercise of its discretion may seek guidance in appellate court decisions that set forth guidelines for trial courts to follow in exercising their discretion to award prejudgment interest in federal question and admiralty cases. For example, the guidelines set forth by the federal Court of Appeals for the Seventh Circuit call upon the district courts to award prejudgment interest at the market rate, which may be either (a) the actual rate that the losing party must pay to borrow money or (b) the U.S. prime rate, which is a market-based estimate. Counsel may wish to alert arbitrators to this case law and/or to the various approaches that economists employ in calculating the amount of prejudgment (or pre-award) interest necessary to compensate the prevailing party for the loss of use of its money.

Summaries of arbitral awards set forth in Appendix A to this report suggest that uncertainty exists with respect to the criteria that international arbitrators should apply in determining pre-award and post-award interest. International arbitrators generally give effect to contractual stipulations on interest; however, arbitral practice varies with respect to the determination of interest in the absence of such stipulations. Arbitrators in a significant minority of the surveyed awards expressly determined that New York’s nine percent prejudgment interest

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3 In re Oil Spill by the Amoco Cadiz, 954 F.2d 1279, 1331-35 (7th Cir. 1992).
provisions do not apply to the determination of interest in international arbitration. A majority of the awards surveyed awarded interest, typically with little or no analysis, in accordance with New York’s prejudgment interest provisions. The Committee hopes that this report will serve to enhance consistency and predictability in the analysis underpinning the award of interest in international arbitrations governed by New York substantive law.

II. Standards Governing the Award of Interest by International Arbitrators

Generally, interest on amounts awarded in arbitration may accrue during three periods: (a) the period from the date the prevailing party’s claim arose to the date of the award (pre-award interest); (b) the period from the date of the award to the date of entry of judgment enforcing the award (post-award, prejudgment interest); and (c) the period from the date of entry of judgment to the date of payment (post-judgment interest).

The confidentiality of the arbitral process presents an obstacle to the collection of reliable statistics. The summaries of awards set forth in Appendix A indicate, however, that commercial arbitrators grant pre-award interest to the prevailing party as a matter of course and sometimes grant post-award, prejudgment interest.

A. Pre-Award Interest

Recent commentaries on the award of interest in international arbitration illustrate the complexity of the subject and prompt this Committee to propose that, in international commercial arbitration governed by New York substantive law, arbitrators apply a step-by-step approach to their determination of pre-award interest.

See Appendix A, rows 1 to 8.

See id., rows 17 to 42.

See, e.g., GARY B. BORN, INTERNATIONAL COMMERCIAL ARBITRATION 3105 (2014) (“The interplay between differing national laws dealing with interest, as well as national characterizations of interest rules and national choice-of-law rules, can be metaphysical in their theoretical complexity.”); Thierry J. Senechal & John Y. Gotanda, Interest as Damages, 47 COLUMBIA J. TRANSNAT’L L. 491 (2009); Andrea Giardina, Issues of Applicable

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The standards that govern the pre-award interest determination in any given arbitration will depend on factors including (a) the terms of the parties’ contract, (b) the applicable arbitration rules, (c) the law governing the merits, and/or (d) the applicable arbitration law. The Committee proposes that arbitrators prioritize these factors according to how clearly and directly each factor reflects the intent of the parties as to the principles that should govern in the event of an arbitrated dispute between them. The recommended order of priority acknowledges and gives effect to (a) the contracting parties’ broad autonomy, under the law of international commercial arbitration applicable in New York, to agree on the law and procedures that apply to their dispute, and (b) the emphasis in the New York law of contract interpretation on construing agreements in accordance with the parties’ intent as expressed in the language of their agreement.7

Each step in the Committee’s suggested methodology is explained *seriatim* below. The last subsection (subsection II.A.5) provides general guidelines that arbitrators may decide to follow in exercising the discretion that they will often possess with respect to the determination of pre-award interest in arbitrations governed by New York substantive law.

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7 See, e.g., *Born*, supra note 6 at 102 (noting the New York Convention’s “emphatic recognition of the predominant role of party autonomy in the arbitral process”); *Sec. Ins. Co. of Hartford v. TIG Ins. Co.*, 360 F.3d 322, 325 (2d Cir. 2004) (Federal Arbitration Act “requires arbitration proceed *in the manner provided for in the parties’ agreement*”) (internal quotation marks, alteration and citation omitted; emphasis in original); *Greenfield v. Phillies Records, Inc.*, 98 N.Y.2d 562, 569 (2002) (“The fundamental, neutral precept of contract interpretation is that agreements are construed in accord with the parties’ intent.”) (citation omitted); *Slatt v. Slatt*, 64 N.Y.2d 966, 967 (1985) (“In adjudicating the rights of parties to a contract, courts . . . are required to discern the intent of the parties[].”)
1. **Contractual Stipulations on Interest**

The first step in the Committee’s suggested methodology is for arbitrators to determine whether the parties’ contract establishes how interest is to be assessed in the arbitration. Subject to limited exceptions discussed below, contractual stipulations governing the assessment of interest on the damages awarded by a court or tribunal are valid and enforceable under the laws of most jurisdictions (including New York).  

Contracts occasionally include a clause that specifically sets the rate of interest on damages or on a particular category of damages. If the contract contains such a clause, and if the clause applies to the damages awarded, it is appropriate for arbitrators to determine pre-award interest in accordance with it, subject to the considerations discussed below. More often, the parties’ contract will contain a “late payment” clause or other similar type of clause stipulating how interest is to be assessed on amounts past due under the contract. Such a clause typically addresses such matters as when interest begins to accrue on an amount due, the rate at which it accrues, whether the interest is simple or compound, and, if it is compound, the compounding period.

In the Committee’s view, generally it is appropriate for arbitrators to apply a late payment or other similar clause if the losing party’s breach consists of a failure to make or delay

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8. See, e.g., *NML Capital v. Republic of Argentina*, 17 N.Y.3d 250, 258 (2011) (*NML I*) (“When a claim is predicated on a breach of contract, the applicable rate of prejudgment interest varies depending on the nature and terms of the contract.”); 10 J. B. WEINSTEIN, H. L. KORN & A. R. MILLER, *NEW YORK CIVIL PRACTICE § 5004.01a, at 50-79 (2016* (“The parties may establish, by contract, the rate of interest to be paid until entry of judgment[,]”); English Arbitration Act 1996, § 49(1) (“The parties are free to agree on the powers of the tribunal as regards the award of interest.”).

9. Following is an example of a clause addressing the assessment of interest on a particular category of damages: “[Any amount of unpaid Seller Damages] that is ultimately determined to have been due on any Damages Due Date shall bear interest at the Default Rate . . . from such Damages Due Date until the date of payment.”

10. Following is an example of a late payment clause: “Unless otherwise specified, all sums due under the Contract shall be paid within forty five (45) days from the date on which the obligation to pay was incurred. All sums due by one Party to the other under the Contract shall, for each day such sums are overdue, bear interest compounded daily at the applicable LIBOR plus two (2) percentage points.”
in making a required payment under the contract. Arbitrators should exercise caution, however, in deciding whether to grant pre-award interest in accordance with a late payment clause on damages awarded for breaches of contract not involving non-payment or late payment. If an arbitral tribunal decides that an interest rate in a late payment clause is not relevant to the determination of pre-award interest on damages awarded for other kinds of breaches, the arbitrators should proceed to the next step in the methodology suggested herein.

In certain limited circumstances, arbitrators may decline to award interest in accordance with a contractual stipulation. For example, if a contractual stipulation on interest is invalid under the usury law of the jurisdiction whose law governs the parties’ contract, arbitrators should decline to enforce the stipulation and consider other methods of calculating interest. Usury laws may be subject, however, to exceptions rendering them inapplicable to pre-award and post-award interest. For example, New York’s civil usury law, which prohibits charging more than sixteen percent interest per year, does not preclude applying a contractually stipulated rate to pre-award and post-award interest in a commercial dispute because the usury law does not apply to interest on defaulted obligations.

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11 See, e.g., Allenby, LLC v. Credit Suisse AG, 25 N.Y.S.3d 1, 6 (1st Dep’t 2015) (contractual stipulation on interest applied only to delayed settlement, not damages awarded by court for breach of contract); Ross v. Ross Metals Corp., 976 N.Y.S.2d 485, 487-88 (2d Dep’t 2013) (contractual stipulation on interest was basis for calculating monthly payments due under contract, but did not apply to damages awarded by court for defendant’s breach of its obligation to make such payments); NML I, 17 N.Y.3d at 261-62 (clause in bond documents providing that interest would accrue at specified rate “until the principal is paid” applied to damages awarded by court for Argentina’s breach of its obligation to make bi-annual interest payments to bondholders). In drafting a late payment or other similar clause, contract drafters may wish to make clear whether the clause is intended to apply to the determination of interest on the damages awarded for a contractual breach not consisting of a failure to make a required payment or of a delay in making a required payment.

12 The validity of a contractual stipulation on interest is generally determined by the law governing the parties’ contract. See Restatement (Second) Conflict of Laws § 207 cmt. e (1971) (“[The law governing the parties’ contract] determines the validity of an express contractual provision for the payment of a stipulated rate of interest.”); DICEY, MORRIS & COLLINS ON THE CONFLICT OF LAWS (15th ed.) § 7-089 (“[W]hether an express undertaking to pay interest is lawful or whether it is made invalid wholly or partly by legislation referring to usury or money-lending depends on whether that legislation forms part of the law applicable to the contract.”).

13 See, e.g., Bloom v. Trepmal Constr. Corp., 289 N.Y.S.2d 447, 448 (2d Dep’t 1968), aff’d, 23 N.Y.2d 730 (1968) (provision in note fixing interest due after default at rate in excess of statutory maximum was valid and
In addition, the public policy of some countries may prohibit the charging of any interest or the charging of interest at a high rate.\textsuperscript{14} If an arbitration is seated in such a country, or if enforcement is likely to be sought in such a country, the tribunal may decline to give effect to an otherwise valid contractual stipulation on interest in order to minimize the risk that its award will be vacated (annulled) by a court of the seat or denied enforcement in other courts on public policy grounds.\textsuperscript{15} Alternatively, arbitrators may issue a partial award granting the principal amount of damages and a separate partial award granting interest as a possible device to insulate the former award from vacatur at the seat or a refusal to enforce on public policy grounds.\textsuperscript{16}

2. \textbf{Arbitration Rules}

The second step in the Committee’s suggested methodology, to be followed if the parties’ contract does not contain a provision governing the assessment of interest on damages awarded,
is for arbitrators to look to the arbitration rules chosen by the parties for any provisions regarding the award of interest. The rules of several leading international arbitral institutions grant arbitrators discretion to award such interest as they consider appropriate.\textsuperscript{17} For example, Article 31(4) of the International Arbitration Rules (the “Rules”) of the American Arbitration Association’s International Centre for Dispute Resolution (the “ICDR”) (“ICDR Article 31(4)”) provides as follows: “[T]he tribunal may award such pre-award and post-award interest, simple or compound, as it considers appropriate, taking into consideration the contract and applicable law(s).” By contrast, the UNCITRAL Arbitration Rules and the rules of several other leading institutions, including the ICC, Hong Kong International Arbitration Centre (the “HKIAC”) and Swiss Chambers, are silent with respect to the award of interest.

In view of the frequent use of the ICDR Rules in international commercial arbitrations governed by New York substantive law, the requirement under ICDR Article 31(4) that the tribunal “take into consideration the contract and applicable law(s)” in exercising its discretion to award interest raises three noteworthy issues.\textsuperscript{18} First, arbitrators might well ponder the meaning of “taking into consideration the [parties’] contract.” In the Committee’s view, if the contract contains a clause that specifically addresses the assessment of interest on the amounts

\textsuperscript{17} See ICDR International Arbitration Rules, Art. 31(4) (quoted in text); LCIA Arbitration Rules, Art. 26.4 (“Unless the parties have agreed otherwise, the Arbitral Tribunal may order that simple or compound interest shall be paid by any party on any sum awarded at such rates as the Arbitral Tribunal decides to be appropriate (without being bound by rates of interest practised by any state court or other legal authority) in respect of any period which the Arbitral Tribunal decides to be appropriate ending not later than the date upon which the award is complied with.”); SIAC Arbitration Rules, Rule 32.9 (“The Tribunal may award simple or compound interest on any sum which is the subject of the arbitration at such rates as the parties may have agreed or, in the absence of such agreement, as the Tribunal determines to be appropriate in respect of any period which the Tribunal determines to be appropriate.”); WIPO Arbitration Rules, Art. 62(b) (“The Tribunal may award simple or compound interest to be paid by a party on any sum awarded against that party. It shall be free to determine the interest at such rates as it considers to be appropriate, without being bound by legal rates of interest, and shall be free to determine the period for which the interest shall be paid.”); JAMS International Arbitration Rules, Art. 35.7 (same as Article 31(4) of ICDR Rules); DIFC-LCIA Arbitration Rules, Art. 26.4 (same as Article 26.4 of LCIA Rules).

\textsuperscript{18} This language is repeated in the September 2016 revisions to the JAMS International Arbitration Rules. See JAMS International Arbitration Rules, Art. 35.7.
awarded, respect for party autonomy typically would suggest that arbitrators determine interest in accordance with that clause rather than exercise their discretion under ICDR Article 31(4), at least in part because “specific terms [of a contract] . . . are given greater weight than general language.” The reference to “taking into consideration” the parties’ contract in ICDR Article 31(4) appears to acknowledge that an arbitral tribunal has discretion to consider whether to determine interest in accordance with a contractual stipulation on interest, such as a late payment clause, that does not strictly apply, by its terms, to damages awarded for reasons other than late payment.

Second, arbitrators may wish to consider what laws are included within the term “applicable law(s)” in ICDR Article 31(4). In the Committee’s view, the term includes the substantive law(s) governing the parties’ contract. The Committee considers that the term “applicable laws(s)” may be understood also to include the arbitration law of the arbitral seat when it addresses an arbitral tribunal’s remedial powers. In addition, arbitrators exercising discretion under ICDR Article 31(4) may take into consideration the public policies of the arbitral seat and of any jurisdiction where the award is likely to be enforced, even though such

19  RESTATEMENT (SECOND) OF CONTRACTS § 203(c) (1981). See generally County of Suffolk v. Long Island Lighting Co., 266 F.3d 131, 139 (2d Cir. 2001) (“It is axiomatic that courts construing contracts must give specific terms and exact terms greater weight than general language.”) (internal quotation marks, ellipsis and citations omitted).
20  See, e.g., ICC Award No. 7622, ICC International Court of Arbitration Bulletin 15(1) (2004), at 79 (applying contract rate even though it did not apply to damages awarded); ICC Award No. 6219, ICC International Court of Arbitration Bulletin 3(1) (1992), at 22 (same). See also Secomb, supra note 6, at 432.
21  Paragraph (1) of Article 31 provides in pertinent part that “[t]he arbitral tribunal shall apply the substantive law(s) or rules of law agreed by the parties as applicable to the dispute.” Prior to the 2014 revisions to the ICDR Rules, the predecessor article to ICDR Article 31(4) required that the tribunal take into consideration the contract and “applicable law” (singular). See ICDR International Arbitration Rules (as amended and effective June 1, 2009), Art. 28(4). No commentary on the 2014 revisions to the Rules addresses the change from the singular to the optional plural in the interest provision.
22  See subsection II.A.4 below.
public policies might not be viewed as falling within the ordinary meaning of “applicable law(s).”

Third, when “taking into consideration the . . . applicable law(s)” in accordance with ICDR Article 31(4), arbitrators may wish to consider what effect they should give to the law governing the parties’ contract. As discussed in subsection II.A.3 below, many jurisdictions have enacted statutory provisions specifying how interest shall be assessed on the damages component of court judgments. Arbitrators exercising their discretion under ICDR Article 31(4) may deliberate on the meaning of “taking into consideration” such statutory provisions. The question takes on practical significance when the statutory provisions call for the application to court judgments of a rate of interest that materially overcompensates or undercompensates the prevailing party in light of prevailing market rates of interest or the prevailing party’s actual cost of funds.

In the Committee’s view, ICDR Article 31(4) allows an arbitral tribunal, in the exercise of its discretion, to determine pre-award and post-award interest wholly or partially in accordance with the statutory prejudgment interest provisions applicable to court judgments.

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23 The same question could be asked with respect to the arbitration law of the seat. As discussed in subsection II.A.4 below, however, all of the arbitration laws surveyed that address the awarding of interest either (a) grant the tribunal discretion to award such interest as it considers appropriate or (b) provide that the tribunal may award interest, without addressing the standard that the tribunal should apply in making such an award. Accordingly, no conflict generally will arise between the standard for awarding interest under Article 31(4) of the ICDR Rules and the standard for awarding interest under the arbitration law of the seat.

24 New York’s statutory prejudgment interest rate of nine percent, enacted by the NY Legislature when market rates were even higher, exceeds market rates of interest generally prevailing in the United States at the time of this report. By contrast, the statutory interest rates of some other jurisdictions may be set below commercially available rates. For example, the French Civil Code allows for the award of simple interest at the “legal rate,” which is fixed by the French Minister of Economy every six months based on the European Central Bank’s benchmark rate and commercial lending rates in France. *See CODE CIVIL [C. CIV.] art. 1231-7 (Fr.); Decree No. 2014-947 of August 20, 2014 Relating to the Legal Rate of Interest (amending Article L. 313-2 of the Monetary and Financial Code).* As of June 2017, the French legal rate was only 0.90% per year. Some jurisdictions have adopted a statutory prejudgment interest rate that continuously floats by reference to a benchmark rate. For example, the Delaware Code provides for a “legal rate” of five percent over the Federal Reserve discount rate. *See DEL. CODE ANN. tit. 6, § 2301(a).* The Delaware courts generally award prejudgment interest at the legal rate defined by Section 2301(a). *See, e.g., Montgomery Cellular Holding Co. v. Dobler, 880 A.2d 206, 226 (Del. 2005) (“the legal rate [defined by Section 2301(a)] has historically been considered as the ‘benchmark’ for prejudgment interest”).*
under the law governing the parties’ contract. For example, if interest only begins to accrue under that law from the date of a formal demand for payment, arbitrators would have discretion to award interest from that date; at the same time, they could determine the interest rate based on commercial considerations and without regard for any statutory prejudgment interest rate under the applicable law.

An arbitral tribunal would also have discretion, in the Committee’s view, to award interest under ICDR Article 31(4) based exclusively on commercial considerations and without any regard for statutory interest provisions applicable to court judgments under the law governing the parties’ contract. In the Committee’s view, an award of interest based exclusively on commercial considerations would be in accord with party expectations that reasonably arise (subject to specific evidence to the contrary) from ICDR Article 31(4)’s grant of discretion to the tribunal to award such interest “as it considers appropriate.”

3. **Law Governing the Merits**

Courts have held that the purpose of pre-award interest is to compensate the prevailing party for the loss of use of money that the prevailing party was entitled to receive from the date its claim arose until the date of the award. Because pre-award interest is an element of

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25 Subsection II.A.5 below sets forth general guidelines that a tribunal may choose to follow in determining an appropriate interest rate, whether interest is simple or compound, and, if compound, the compounding period.

26 See, e.g., NML I, 17 N.Y.3d at 266 (“[T]he function of prejudgment interest is to compensate the creditor for the loss of use of money the creditor was owed during a particular period of time.”) (internal citations omitted); Kassis v. Teachers’ Ins. & Annuity Ass’n, 786 N.Y.S.2d 473, 474 (1st Dep’t 2004) (“The purpose of prejudgment interest is to compensate parties for the loss of the use of money they were entitled to receive, taking into account the time value of money.”) (internal quotation marks and citation omitted).
complete compensation for the claim, the Committee’s view is that it should generally be determined in accordance with the same law that governs liability and damages.

This choice-of-law approach accords with New York’s choice-of-law rules. It also accords with Comment (e) to Section 207 of the Restatement (Second) of Conflict of Laws, which provides that the law governing the parties’ contract “determines whether plaintiff can

27 See, e.g., West Virginia v. United States, 479 U.S. 305, 310 (1987) ("Prejudgment interest is an element of complete compensation."). In the international context, see 2010 UNIDROIT PRINCIPLES OF INTERNATIONAL COMMERCIAL CONTRACTS ("UNIDROIT PRINCIPLES") Art. 7.4.2(1) ("The aggrieved party is entitled to full compensation for harm sustained as a result of the non-performance.").

28 Most international arbitration rules grant arbitrators discretion to apply the law or rules of law they determine to be appropriate, in the absence of party agreement as to the applicable law. See, e.g., ICDR Arbitration Rules, Art. 31(1) ("Failing such an agreement by the parties [on the substantive law(s) or rules of law applicable to the dispute], the tribunal shall apply such law(s) or rules of law as it determines to be appropriate."); ICC Arbitration Rules, Art. 21(1) ("In the absence of any such agreement [on the rules of law applicable to the merits of the dispute], the arbitral tribunal shall apply the rules of law which it determines to be appropriate."). International arbitrators reasonably may conclude that a generic choice-of-law clause specifying the law governing the parties’ contract does not encompass an agreement that that law shall govern the determination of pre-award interest, given that interest is generally considered as incidental to the damages awarded on the main claim. Cf. Mastrobuono v. Shearson Lehman Hutton, Inc., 514 U.S. 52, 58-64 (1995) (interpreting generic choice-of-law clause referring to “the laws of the State of New York” as encompassing New York’s substantive rights and obligations, but not its prohibition on the award of punitive damages by arbitrators). Nonetheless, as explained in this subsection, it would generally be appropriate for international arbitrators to determine pre-award interest in accordance with the law governing the parties’ contract, because interest is an element of complete compensation for the main claim.

Gary Born distinguishes, for choice-of-law purposes, between an arbitral tribunal’s authority to award interest and the standards governing the exercise of that authority. Born, supra note 6 at 3103-06. According to Professor Born, “the better view appears to be that, absent contrary agreement, questions concerning the arbitrators’ authority to award interest are better regarded as subject to the law of the arbitral seat” because “[i]t is that law which is generally regarded as having the closest connection to questions concerning the tribunal’s powers.” Id. at 3104. As discussed in subsection II.A.4.a below, both federal and New York arbitral law grant arbitrators broad remedial powers that include the power to award interest, absent party agreement to the contrary. Professor Born further suggests that international arbitrators should “apply the law of the currency in which any award is made to determine the substantive standards, including the applicable interest rates, for any award of interest,” although he recognizes that “arbitrators have in practice generally looked to the substantive law governing the parties’ underlying claims for standards regarding interest.” Id. at 3105-06.

29 See, e.g., Schwimmer v. Allstate Ins. Co., 176 F.3d 648, 650 (2d Cir. 1999) ("Under New York choice of law rules, the law of the jurisdiction that determines liability governs the award of pre-judgment interest."); Davenport v. Webb, 11 N.Y.2d 392, 394-95 (1962) (prejudgment interest is substantive issue controlled by law governing merits); Sirie v. Godfrey, 196 A.D. 529, 539 (1st Dep’t 1921) (entitlement to prejudgment interest was governed by French law, which was law governing parties’ contract). The choice-of-law rules of some other jurisdictions may treat prejudgment interest as a procedural matter governed by the law of the forum. See Born, supra note 6, at 3105.
recover interest, and, if so, the rate, upon damages awarded him for the period between the breach of contract and the rendition of judgment.”

a. **New York Substantive Law Relating to the Award of Interest by International Arbitrators**

If New York substantive law governs the merits of the parties’ dispute, international arbitrators should consider what standards, if any, that law imposes on the award of interest in international arbitration. One question that frequently arises in practice is whether New York’s prejudgment interest provisions contained in C.P.L.R. Sections 5001, 5002 and 5004 apply to the determination of interest in arbitration. For the reasons set forth in this subsection, it is the Committee’s view that international arbitrators (a) are not bound to apply these provisions and (b) have discretion under New York’s substantive common law to award such interest as they consider appropriate.

i. **Inapplicability of New York’s Prejudgment Interest Provisions to International Arbitration**

C.P.L.R. Sections 5001, 5002 and 5004 provide for mandatory prejudgment interest, at an annual rate of nine percent and on a simple-interest basis, upon any sum awarded by a New York State court for breach of contract. Although these provisions are found in the Civil Practice Law and Rules, state and federal courts have found them to be substantive for choice-of-law and *Erie* purposes. Whether these statutory prejudgment interest provisions apply in arbitration

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30 *Restatement (Second) Conflict of Laws* § 207 cmt. e (1971). See also id. § 171 cmt. c (law governing tort liability and damages “determines whether the plaintiff can recover interest and, if so, at what rate for a period prior to the rendition of judgment as part of the damages for a tort”).


32 See, e.g., *Davenport*, 11 N.Y.2d at 394-95 (prejudgment interest is substantive issue controlled by law governing merits); *Paine Webber Jackson & Curtis, Inc. v. Winters*, 579 A.2d 545, 551-53 (Conn. App. Ct. 1990) (N.Y.C.P.L.R. § 5001 is rule of substantive law to be applied by Connecticut courts if New York law governs merits); *Schwimmer*, 176 F.3d at 650 (prejudgment interest is substantive issue for *Erie* purposes). See also *Restatement (Second) Conflict of Laws* § 207 cmt. e (1971); id. § 171 cmt. c. Under the *Erie* doctrine, a U.S. federal court hearing a claim brought under state law must apply state rules that the court considers “substantive”
does not turn, however, on whether they are characterized as substantive or procedural for purposes of determining their applicability in state or federal court.\textsuperscript{33} Rather, the Committee considers the key question to be whether the provisions are directed to the determination of interest not only by a court, but also by arbitrators. As shown by the summaries of awards in Appendix A of this report, arbitrators have not always considered this question or answered it in a consistent manner.

In the Committee’s view, based upon the statutory language and New York case law, New York’s statutory prejudgment interest provisions are binding only in court proceedings and not in arbitration. Several sections of the C.P.L.R. support this conclusion. First, C.P.L.R. Section 101 provides that the Civil Practice Law and Rules “shall govern the procedure in civil judicial proceedings in all courts of the state and before all judges.”\textsuperscript{34} The inclusion of New York’s prejudgment interest provisions in a statute that governs civil proceedings in the courts of the state and before “all judges” indicates that the NY Legislature intended for the interest provisions to be applicable in court proceedings, not in arbitration. The C.P.L.R. does address certain limited aspects of arbitration in its Article 75, generally considered to be the first under federal law, while applying federal rules that it considers “procedural” under federal law. See Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938). It is beyond the scope of this report to address whether courts outside the United States apply New York’s prejudgment interest provisions if New York substantive law governs the merits of the parties’ dispute.

\textsuperscript{33} One reason courts have characterized statutory prejudgment interest provisions as substantive for choice-of-law and \textit{Erie} purposes is to discourage forum shopping by plaintiffs, who otherwise might choose to sue in a particular court to take advantage of that forum’s statutory prejudgment interest rate. See, e.g., Jarvis v. Johnson, 668 F.2d 740, 745 (3d Cir. 1982) (“[I]f [Pennsylvania’s prejudgment interest statute] is not applied in the federal courts, an incentive for forum shopping in diversity actions may well result. We can readily foresee that many plaintiffs would sue in Pennsylvania state court to take advantage of [Pennsylvania’s prejudgment interest statute] and thus to recover considerable additional damages.”). This anti-forum-shopping rationale does not support the application of statutory prejudgment interest provisions in arbitration, however, because the parties to an arbitration agreement cannot shop for a forum after the agreement to arbitrate has been signed. And unlike the rules that govern court jurisdiction, the parties’ choice of a seat of arbitration in international arbitration frequently reflects a determination that the seat has \textit{no} connection with the parties or the dispute. There is, therefore, little reason for an arbitral tribunal to reach the same result that a court at the seat would reach.

\textsuperscript{34} N.Y.C.P.L.R. Section 105(d) defines “civil judicial proceeding” as “a prosecution, other than a criminal action, of an independent application to a court for relief.”
arbitration statute in the United States and a model used in the drafting of the Federal Arbitration
Act. Article 75 makes no reference, by cross-reference or otherwise, to the issue of interest
awards in arbitration.

Second, New York’s prejudgment interest provisions are part of C.P.L.R. Article 50, entitled
“Judgments Generally.” N.Y.C.P.L.R. Section 5011 defines “judgment” as “the
determination of the rights of the parties in an action or special proceeding and may be either
interlocutory or final.” Arbitration does not qualify as an “action” or as a “special proceeding”
under the N.Y.C.P.L.R. The inclusion of the prejudgment interest provisions in an article
relating to “judgments” is a further indication that the NY Legislature intended for the interest
provisions to apply only to civil proceedings in New York State’s courts.

Third, N.Y.C.P.L.R. Sections 5001 and 5002 contain numerous terms indicating that they
are intended to apply only in court proceedings. Subdivision (a) of Section 5001 provides, in
full, as follows:

**Actions in which recoverable.** Interest shall be recovered upon a sum awarded
because of a breach of performance of a contract, or because of an act or omission
depriving or otherwise interfering with title to, or possession or enjoyment of,
property, except that in an action of an equitable nature, interest and the rate and
date from which it shall be computed shall be in the court’s discretion.

Subdivision (a) thus refers to “action[s]” both in its title and in its text. As already noted,
arbitration does not qualify as an “action” under the C.P.L.R. The reference to the “court’s
discretion” to award interest in equitable actions further suggests that the NY Legislature, in its
enactment of Section 5001, considered only court proceedings. So, too, do the references in
subdivisions (b) and (c) of Section 5001 and in Section 5002 to “the cause of action,” “the jury,”
“the court,” “motion,” “the clerk of the court” and “any action.”

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36 See, e.g., N.Y.C.P.L.R. §§ 103(b), 105(b), 304, 7502(a).
The legislative history of C.P.L.R. Section 5004, which fixes the prejudgment interest rate applicable under Sections 5001 and 5002 at nine percent, further supports the conclusion that these sections are intended to apply only in court proceedings, not in arbitration. The NY Legislature adopted the fixed nine percent rate in part for reasons not directly related to the compensatory purpose of an interest award and not necessarily relevant to the award of interest in international arbitration.

The highest court of the State of New York, the New York Court of Appeals ("NY Court of Appeals") explained as follows:

Prior to 1972, CPLR 5004 provided that “[i]nterest shall be at the legal rate, except where otherwise prescribed by statute.” The “legal rate” was then based upon the variable rate of interest on the loan or forbearance of money as set by the Banking Board, or, if no rate had been prescribed by the Banking Board, the rate of 6% per annum (see, 1972 Report of NY Law Rev Commn, 1972 NY Legis Doc No. 65 [C], reprinted in 1972 McKinney’s Session Laws of NY, at 3226). However, in its review of the provision, the Law Revision Commission recommended that the rate be fixed at 6% based upon the following reasons: (1) 6% was the historical rate from 1879; (2) the interest rate for a loan or forbearance was not logically or necessarily related to the rate for judgments; (3) a fixed rate would facilitate the administrative act of entering judgments with interest “without possible controversy over different rates for different periods;” and (4) the power of the Banking Board to set such rates was due to expire later that year. Accordingly, in 1972, CPLR 5004 was amended to set a fixed interest rate on judgments at “six per centum per annum” (L 1972, ch 358).

However, in the years that followed, interest rates soared in an inflationary market. The 1981 Report of the Advisory Committee on Civil Practice noted reports where defendants had exploited the system by investing and accruing interest on funds which would otherwise have been used to pay judgment creditors (1981 McKinney’s Session Laws of NY, at 2658). Increased returns were facilitated through such delaying tactics as “the prosecution of unmeritorious appeals and eschewing reasonable settlements” (Mem of Assemblyman Goldstein, 1981 NY Legis Ann, at 148). Although arguments had been made “to reinstate the market rate under CPLR 5004” (1981 McKinney’s Session Laws of NY, at 2658; see also, Siegel, Practice Commentaries, McKinney’s Cons Laws of NY, Book 7B, CPLR 5004), the Advisory Committee then recommended increasing the fixed rate payable on judgments from 6 to 9%. The recommendation was enacted in 1981 (see, L 1981, ch 258) and the rate has remained unchanged since.
Rodriguez v. New York City Housing Authority, 91 N.Y.2d 76, 78-79 (1997). The NY Legislature thus appears to have adopted a fixed rate of six percent in 1972 based upon a complex set of public policy goals not all of which were directly related to determining an appropriate level of compensation in a particular case. In 1981, after market rates had risen into the high teens, the NY Legislature increased the fixed rate from six percent to nine percent, in part, to discourage defendants from using delay tactics in court proceedings.

The NY Court of Appeals has not had occasion to address squarely the applicability, or not, of New York State’s prejudgment interest provisions to international or domestic arbitration. It can reasonably be surmised that this is due, at least in part, to the very limited grounds available to challenge an arbitral award or to resist its enforcement. New York’s courts have consistently rejected, however, applications to modify an award or to grant pre-award interest in circumstances where the award allegedly did not comply with New York’s prejudgment interest provisions.

The leading case in this area is Penco Fabrics, Inc. v. Bogopulsky, Inc., 146 N.Y.S.2d 514 (1st Dep’t 1955), in which the Appellate Division, First Department, held that “[t]he right to interest involves questions of fact and law that are within the purview of the arbitrators.” Id. at 515. The arbitral tribunal had awarded damages for breach of contract, but it had not granted any pre-award interest, even though Section 480 of the then Civil Practice Act, the predecessor to C.P.L.R. Section 5001, provided for mandatory prejudgment interest in breach of contract

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37 The six percent rate adopted in 1972 was close to the market rates in effect at the time. During 1972, the U.S. prime rate ranged from 4.50% to 6.00%. See http://www.fedprimerate.com/wall_street_journal_prime_rate_history.htm.

38 During 1981, the U.S. prime rate ranged from 15.75% to 21.50%. See id.
actions.  

The Appellate Division denied the award-creditor’s request for pre-award interest, reasoning as follows:

The mere fact that the award was silent on the question did not mean that the arbitrators did not consider the question and did not operate to enable the court to allow such interest. Provisions of law applicable to judicial actions and proceedings do not necessarily apply to arbitrations. Parties who submit their controversies to arbitration forego those provisions and leave all questions of law and fact to the arbitrators.

Id. The Appellate Division characterized the grant of pre-award interest as a mixed question of law and fact for the tribunal to decide and held that a tribunal’s decision on that question is not subject to review by the courts.  

Three Appellate Division cases holding that a domestic arbitral tribunal’s power to grant pre-award interest stems from its broad remedial powers under New York arbitral law (without any mention of C.P.L.R. Section 5001) support the conclusion that New York State’s prejudgment interest provisions do not apply in arbitration.  

Levin & Glasser, P.C. v. Kenmore Property, LLC, 896 N.Y.S.2d 311 (1st Dep’t 2010), is typical of these three cases. The award-creditor in Levin & Glasser requested that the court grant pre-award interest on the damages

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39 Section 480 of the then Civil Practice Act provided as follows:

In every action wherein any sum of money shall be awarded by verdict, report, or decision upon a cause of action for the enforcement of or based upon breach of performance of a contract, express or implied, interest shall be recovered upon the principal sum, whether theretofore liquidated or unliquidated, and shall be added to and be a part of the total sum awarded.

N.Y. Civil Practice Act § 480 (as amended in 1927).

40 In subsequent cases, the Appellate Division has reaffirmed that “in a contract dispute brought before an arbitrator[,] the question of whether interest from the date of the breach of the contract should be allowed in an arbitration award is a mixed question of law and fact for the arbitrator to determine.” Levin & Glasser, P.C. v. Kenmore Property, LLC, 896 N.Y.S.2d 311, 312 (1st Dep’t 2010) (internal quotation marks, alteration and citation omitted). See also, e.g., Dermigny v. Harper, 6 N.Y.S.3d 561, 562 (2d Dep’d 2015) (“[B]ecause the arbitration award did not include a provision awarding the defendant [pre-award] interest, the court was without power to award [such] interest.”); Rothermel v. Fidelity & Guarantee Ins. Underwriters, Inc., 721 N.Y.S.2d 565, 566 (3d Dep’t 2001) (“the question as to whether pre-award interest is to be allowed is for the arbitrator to determine”); Gruberg v. Cortell Group, Inc., 531 N.Y.S.2d 557, 558 (1st Dep’t 1988).

awarded by the tribunal, contending that the tribunal had lacked the authority to award interest under the arbitration rules of New York’s Fee Dispute Resolution Program, which are silent on this issue. *Id.* at 312-13. The Appellate Division rejected this contention on the ground, *inter alia*, that a tribunal’s “broad authority to resolve disputes” under New York arbitral law includes the power to award interest. *Id.* The fact that the court rested its decision on a tribunal’s broad remedial powers under New York arbitral law rather than on C.P.L.R. Section 5001 suggests that the court did not consider Section 5001 in the context of arbitration.*

Three New York federal district courts appear to have assumed, notwithstanding several reported Appellate Division decisions, that New York State’s prejudgment interest provisions apply in domestic arbitration.* In each case, the award-creditor claimed that the tribunal had “manifestly disregarded” the law by failing to grant pre-award interest in accordance with C.P.L.R. Section 5001. The district courts rejected this argument in each of the three cases on grounds other than the non-applicability of C.P.L.R. Section 5001 in arbitration (a point that does not appear to have been argued).* In view of (a) the principle that, in order to establish manifest

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42 See also *West Side Lofts*, 751 N.Y.S.2d at 476 (arbitrator did not exceed his powers by awarding interest; court did not refer to C.P.L.R. § 5001 but instead cited *Silverman v. Bennor Coats, Inc.*, 61 N.Y.2d 299, 308 (1984), which held that arbitrator “may do justice as he sees it”); *Rosenblum*, 439 N.Y.S.2d at 483 (arbitrators had power to rule on pre-award interest based on their broad power to fashion awards to achieve just results).


44 In *Sayigh*, the district court held that the tribunal had not manifestly disregarded the law because (1) the petitioner’s claim arose under a human rights statute and (2) C.P.L.R. Section 5001(a) requires the award of interest only on sums awarded for breach of contract or interference with property. *Sayigh*, 2015 U.S. Dist. LEXIS 27139, at *35. In *Shamah*, the district court concluded that both arbitral tribunals and federal district courts exercising diversity jurisdiction have discretion to award interest at a rate lower than the applicable state statutory prejudgment interest rate, although it erroneously based that conclusion on a Second Circuit decision which held only that in the narrow circumstances of that particular case, the district court had not abused its discretion by using a rate lower than the applicable Vermont statutory prejudgment interest rate. See *Shamah*, 21 F. Supp. 2d at 217 (citing *Chandler v. Bombardier Capital, Inc.*, 44 F.3d 80, 84 (2d Cir. 1994)). In *Nicoletti*, the district court reasoned that “[a]lthough petitioner’s claim sounded in contract, the arbitrators may have concluded that [his] entitlement was equitable rather than contractual, and that therefore interest was discretionary [under C.P.L.R. Section 5001(a)].” *Nicoletti*, 761 F. Supp. at 315.
disregard of the law, “[t]he governing law alleged to have been ignored by the arbitrators must be well defined, explicit, and clearly applicable”;\(^{45}\) (b) the text of the C.P.L.R.; and (c) the Appellate Division’s observation in *Penco Fabrics* that New York’s prejudgment interest provisions “do not necessarily apply to arbitrations,” 146 N.Y.S.2d at 515, counsel for the award-debtor in each of the three cases had available, in opposition to the manifest disregard challenge, a further argument that C.P.L.R. Section 5001 is not “clearly applicable.”\(^{46}\)

ii. Pre-Award Interest Under New York’s Substantive Common Law

In the Committee’s view, New York’s substantive common law allows an arbitral tribunal to award interest as an element of damages on the main claim(s).\(^{47}\) After the enactment of New York’s first prejudgment interest statute in 1920, New York courts have held that they may award prejudgment interest only on the basis of specific statutory authority.\(^{48}\) Prior to the

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\(^{46}\) In *Moran v. Arcano*, No. 89 Civ 6717, 1990 U.S. Dist. LEXIS 9349 (S.D.N.Y. July 27, 1990), Judge Haight of the District Court for the Southern District of New York stated in *dictum* and without referring to C.P.L.R. Section 5001 that “[w]hether interest is taxed on a claim prior to the entry of an arbitration award is within the discretion of the arbitrators.” *Id.* at *6. Judge Haight thus appears to have concluded, *sub silentio*, that C.P.L.R. Section 5001 does not apply in arbitration. However, neither of the two cases that he cited in support of this statement so held. *See Sun Ship, Inc. v. Matson Navigation Co.*, 785 F.2d 59, 63 (3d Cir. 1986) (holding that district court should have granted post-award, prejudgment interest because, while arbitrators had included pre-award interest in their award, they “lacked authority to decide the entirely separate question of prejudgment interest on the amount confirmed by the district court judgment”); *Brandeis Intsel Ltd. v. Calabrian Chemicals Corp.*, 656 F. Supp. 160, 170 (S.D.N.Y. 1987) (confirming award that included pre-award interest granted by arbitrators under English law; arbitration seated in London and parties’ contract governed by English law).

A Massachusetts appellate court has held squarely that, under Massachusetts law, “[a]n arbitrator’s award of interest, when made as a component of an award, is an integral part of the total remedy that he fashions and, as such, is not subject to the statutory provisions which apply to court-awarded interest on contract claims.” *Blue Hills Reg’l Dist. Sch. Comm. v. Flight*, 409 N.E.2d 226, 235 (Mass. App. Ct. 1980). The Massachusetts statutory prejudgment interest provisions are worded similarly to the New York provisions. *See* MASS. GEN. LAWS ch. 231, § 6C (2016) (“In all actions based on contractual obligations, upon a verdict, finding or order for judgment for pecuniary damages, interest shall be added by the clerk of the court to the amount of damages, at the contract rate, if established, or at the rate of twelve percent per annum from the date of the breach or demand.”).

Some commentators argue that, as a general matter, “[c]laimants would be more accurately compensated for the loss of use of their money if they received interest as damages, as opposed to interest on damages.” *Senechal & Gotanda*, supra note 6 at 514. *See also Secomb*, supra note 6, at 443-44.

\(^{47}\) *See, e.g.*, *In re Brooklyn Navy Yard Asbestos Litig.*, 971 F.2d 831, 851 (2d Cir. 1992) (“The right to interest [under New York law] is purely statutory and in derogation of the common law and it cannot be extended beyond*
enactment of that statute, New York common law allowed courts to award prejudgment interest in breach of contract actions with interest running from the date on which the defendant could have ascertained the damages with reasonable certainty.\textsuperscript{49} The Committee believes that, because New York’s prejudgment interest provisions do not apply in arbitration, the proscription on non-statutory interest under New York law also does not apply in arbitration. Moreover, the availability of pre-award interest under New York’s substantive common law accords both with (a) the historical allowance of prejudgment interest under the common law and (b) the compensatory purpose of such interest.\textsuperscript{50}

In addition, as discussed in subsection II.A.4.a below, federal and New York arbitral law both grant arbitrators broad remedial powers that include the discretionary power to award interest on damages. In the Committee’s view, an arbitral tribunal may consider the law regarding its remedial powers, including its discretionary power to award interest, to be substantive law for purposes of choice-of-law analysis, particularly if the tribunal is seated in a jurisdiction that treats arbitrators’ remedial powers as a question of substantive law.\textsuperscript{51}

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\textsuperscript{49} See, e.g., \textit{Faber v. City of New York}, 222 N.Y. 255, 262 (1918) (“[I]f a claim for damages [on account of breach of contract] represents a pecuniary loss, which may be ascertained with reasonable certainty as of a fixed day, then interest is allowed from that day.”).

\textsuperscript{50} In 1927, the New York State Legislature amended the State’s prejudgment interest statute to allow the courts to award prejudgment interest on the principal amount of damages “whether theretofore liquidated or unliquidated.” Shortly thereafter, the NY Court of Appeals held that retrospective application of the amendment to contracts entered into before its enactment did not violate the non-impeachment clause of the U.S. Constitution because the amendment “prevents an escape . . . from the real obligation to make full compensation for breach of contract” and “vindicates a preexisting right to compensation for breach of contract.” \textit{J.B. Preston Co. v. Funkhouser}, 261 N.Y. 140, 145 (1933).

\textsuperscript{51} See \textit{BORN}, \textit{supra} note 6, at 3068 (“[I]n many jurisdictions, the arbitrators’ remedial powers are treated as an aspect of the substantive dispute between the parties.”).
One question that may arise is whether an international arbitral tribunal, in exercising discretion to award interest under New York law, should apply New York’s prejudgment interest provisions even though they are not directed to the determination of interest by arbitrators. Given that C.P.L.R. Section 5001 has been characterized as substantive for choice-of-law and *Erie* purposes, one might argue that an award of interest under this section ordinarily would accord with the parties’ reasonable expectations if they have chosen New York law as the law governing their relationship. Moreover, the Appellate Division recently stated that New York’s “statutory nine percent rate [is] presumptively fair and reasonable, irrespective of the lower interest rate in the current market,” although it made this statement in an equitable action in which it upheld the trial court’s awarding of six percent interest.\(^{52}\)

Arbitrators have discretion to determine interest based primarily on commercial considerations and to consider New York’s statutory prejudgment interest provisions in the light of commercial realities, for three main reasons.

First, as discussed above, the NY Legislature adopted a fixed nine percent prejudgment interest rate in part for reasons not directly related to the compensatory purpose of an interest award and not necessarily relevant to the award of interest in international arbitration.

Second, the award of nine percent simple interest in accordance with New York’s statutory prejudgment interest provisions may materially overcompensate or undercompensate the prevailing party for the loss of use of its funds.\(^{53}\)

\(^{52}\) *Gourary v. Gourary*, 943 N.Y.S.2d 80, 82 (1st Dep’t 2012).

\(^{53}\) In some cases, even in the current low rate environment, the award of nine percent interest in accordance with New York’s statutory prejudgment interest provisions may *undercompensate* the prevailing party for the loss of use of its funds. As noted above, a court may award only simple interest under C.P.L.R. Sections 5001 and 5004. In the commercial world, however, interest on a debt is almost always compounded; for this reason, an arbitral tribunal exercising its discretionary power to award interest under New York’s substantive common law may choose to award interest on a compound basis. Depending on various factors such as the compounding interval and the length of the pre-award period, compound interest calculated at today’s low market rates may exceed simple interest.
Third, given the broad remedial powers of arbitrators under both federal and New York arbitral law and the many uncertainties at the time of contract regarding possible future disputes, commercial parties and their counsel may reasonably expect an arbitral tribunal to exercise discretion to award such interest as it considers appropriate. Of course, if for any reason the parties express a different expectation, for example by fixing the pre-award interest rate in advance, they are free to do so in their contract or in a stipulation entered during arbitration.\textsuperscript{54}

During a period when New York’s statutory prejudgment interest rate is substantially higher or lower than market rates, factors that may weigh in favor of application of the statutory rate in a specific case may include, in the judgment of the tribunal, a showing of party intent that the statutory prejudgment interest rate be applied; the absence of any case made in favor of applying a different rate; or a lack of significant economic impact on the interest calculation in a particular case. Moreover, if both parties argue that New York’s statutory prejudgment interest provisions govern their respective claims for pre-award interest, a tribunal could reasonably infer agreement between the parties that the statutory prejudgment interest rate applies in their arbitration.\textsuperscript{55}

On the other hand, arbitrators have discretion to consider factors that may weigh against application of New York’s statutory prejudgment interest rate in a time of low market interest rates, including the NY Legislature’s desire to set the prejudgment interest rate at a level close to or below the market rates at the time the statutory rate was chosen; the NY Legislature’s concern calculated at New York’s nine percent statutory prejudgment rate. In the Committee’s view, this possibility confirms that it may be appropriate for arbitrators to award interest based on commercial considerations.

\textsuperscript{54} \textit{See} subsection II.A.1 \textit{supra}.

\textsuperscript{55} Arbitrators may also exercise their discretion to apply New York’s statutory prejudgment interest provisions if they take the view that it would be desirable, as a general matter, that the relief granted coincide precisely with the relief that a court hearing the same claim would grant. In the Committee’s view, a tribunal may consider how a court would decide the same question but retains discretion, under well-settled federal and New York State arbitral law, to consider other factors in shaping the tribunal’s remedy. \textit{See} subsection II.A.4.a below.
for easing administrative burdens on the courts; and the extent to which current market rates of interest may adequately discourage the use of delay tactics in arbitration.56

iii. Inapplicability of Section 5-501(1) of New York’s General Obligations Law to Pre-Award Interest

An arbitral tribunal may also wish to consider whether it would be appropriate to award interest at New York’s statutory default rate of interest for loan obligations, as established by Section 5-501(1) of the State’s General Obligations Law (“G.O.L.”). G.O.L. Section 5-501(1) provides that “[t]he rate of interest, as computed pursuant to this title, upon the loan or forbearance of any money, goods, or things in action . . . shall be six per centum per annum unless a different rate is prescribed in section fourteen-a of the banking law.”

In Sedlis v. Gertler, 554 N.Y.S.2d 614 (1st Dep’t 1990), the Appellate Division held that an arbitrator should have granted pre-award interest at the six percent rate set by G.O.L. Section 5-501(1) because the parties’ contract provided that late payments would bear interest at New York’s “legal rate.” Id. at 616. Relying on C.P.L.R. Section 7511(c)(1), which provides that the court shall modify an award if “there was a miscalculation of figures . . . in the award,” the Appellate Division modified the arbitrator’s award (which granted twelve percent pre-award interest) to provide for interest at the six percent rate. Id. The Appellate Division’s modification

56 New York’s maintenance of the nine percent statutory prejudgment interest rate in the current low rate environment may also be intended to encourage defendants to settle claims brought against them. See Oden v. Schwartz, 71 A.3d 438, 457 (R.I. 2013) (upholding constitutionality of Rhode Island’s statutory prejudgment interest rate of twelve percent in medical malpractice actions on ground that this rate is “rationally related to a legitimate state interest of promoting settlement as well as compensating an injured plaintiff for the loss of the use of money to which he or she is legally entitled”). However, any possible state interest in promoting settlement of claims appears to be related to the efficient administration of justice by the courts and does not reflect a substantive policy favoring plaintiffs over defendants. See Paine Webber, 579 A.2d at 551 (court held that Connecticut’s “offer of judgment” rule, which “provides an economic incentive for parties to settle disputes before trial,” was “procedural rule, punitive in nature, and enacted to promote fair and reasonable pretrial compromises of litigation,” and that it therefore applied to action in Connecticut state court even though New York law governed substantive issues in dispute). In view of the many and varied social policies underlying statutory prejudgment interest rates, arbitrators reasonably may conclude that a statutory prejudgment interest rate binding on courts may or may not be appropriate in a particular case but should not dictate the determination of interest in arbitration.
of the award appears anomalous in the sense that it involved the reversal of a substantive ruling, not the correction of a mere computational error.\textsuperscript{57} The court’s interpretation of G.O.L. Section 5-501(1) as establishing a legal rate of interest of six percent under New York law would appear to support the application of this rate to pre-award interest in arbitration irrespective of whether or not the parties specifically so agreed in their contract.

Three factors militate against the application of the six percent rate established by G.O.L. Section 5-501(1) to pre-award interest in arbitration, absent party agreement that this rate will apply. First, G.O.L. Section 5-501(1) provides that the rate set by that section applies to a “loan or forbearance,” a phrase that does not encompass damages owed by a breaching party.\textsuperscript{58} Accordingly, the text of the statute provides no basis for arbitrators to award interest at the six percent rate, absent party agreement to the contrary.

Second, the majority of courts to have addressed the issue have concluded that the six percent rate set forth in G.O.L. Section 5-501(1) is “superseded” by New York’s maximum interest rate of sixteen percent set by Section 14-a of the Banking Law.\textsuperscript{59} The latter is a usury rate and does not reflect the NY Legislature’s calculation of what rate would make an injured party whole. Accordingly, it would not be appropriate, in the Committee’s view, for arbitrators to award interest at the sixteen percent rate set by Section 14-a, absent clear evidence of party intent that it apply in the circumstances.

Third, to the extent that the six percent rate mentioned in G.O.L. Section 5-501(1) retains any validity, the Committee is not aware of any precedent or other authority supporting the

\textsuperscript{57} See, e.g., Madison Realty Capital, L.P. v. Scarborough-St. James Corp., 25 N.Y.S.3d 83, 85 (1st Dep’t 2016) (“CPLR 7511(c)(1) only authorizes modification of computational errors . . . , not reversal of substantive rulings”).

\textsuperscript{58} See, e.g., Manfra, Tordella & Brookes, 794 F.2d at 63.

award of interest in accordance with G.O.L. Section 5-501(1) in arbitration, absent party agreement that New York’s “legal rate” is applicable. Arbitrators therefore should not presume, solely on the basis of the parties’ choice of New York law as the law governing their contract, that parties intended for the six percent rate to apply to the award of interest.

b. **International Arbitrators Should Align the Rate of Interest With the Currency of the Award**

As already noted, many jurisdictions (including New York, in the case of a court judgment) have enacted statutory provisions specifying how interest shall be assessed on damages, including the rate at which it shall accrue.\(^6^0\) For reasons set forth above, the Committee takes the view that neither the New York prejudgment interest provisions (C.P.L.R. §§ 5001, 5002 and 5004) nor G.O.L. Section 5-501(1) are binding in international arbitration. For purposes of this discussion, the Committee assumes that, under some circumstances, the statutory interest provisions of other jurisdictions may be deemed applicable, as a question of local law or public policy, in a particular international arbitration.

In accordance with the choice-of-law analysis discussed above, the law governing the parties’ contract generally should determine whether the prevailing party may recover interest on damages and, if so, how much.\(^6^1\) An award of interest in accordance with these provisions may not be appropriate, however, if (a) the governing law specifies a legal rate of interest and (b) the arbitral tribunal assesses damages and issues its award in the currency of another jurisdiction. For example, a contract may provide for arbitration in New York, French governing law, and payment in U.S. dollars. If, as would be expected, the arbitral tribunal assesses damages and

\(^{60}\) *See, e.g.*, C. CIV. art. 1231-7 (Fr.) (interest on damages accrues at “legal rate”); Decree No. 2014-947 of August 20, 2014 Relating to the Legal Rate of Interest (amending Article L. 313-2 of the Monetary and Financial Code) (legal rate fixed by French Minister of Economy every six months).

\(^{61}\) *See supra* notes 26-30 and accompanying text.
issues its award in U.S. dollars, the grant of pre-award interest at the French legal rate may not make commercial sense because that rate reflects, *inter alia*, material changes in the value of the Euro over time.\textsuperscript{62} In fairly foreseeable circumstances, therefore, application of the French legal rate to an arbitral award in U.S. dollars could significantly undercompensate or overcompensate the prevailing party for the loss of use of its money.\textsuperscript{63}

Arbitral tribunals may wish to consider at least two factors as they seek to avoid anomalies in the interest rate used to calculate pre-award interest. First, arbitrators may consider whether, as a matter of statutory construction, the legal rate under the governing law does not apply to damages assessed in a foreign currency. As explained by Professor Pierre Mayer:

The arbitrator’s sense of equity can suggest to him that the rule expressed in the applicable law only deals with domestic situations, which allows him to formulate himself the rule that is supposed to apply to international situations. This last device has been used to set aside provisions, which can be found in many national laws, which fix the rate of interest at a certain percentage, regardless of the place of payment and of the currency in which the debt was expressed; indeed, such provisions lead to absurd results when applied to international contracts.\textsuperscript{64}

In the event an arbitral tribunal should determine that the legal rate of interest under the governing law does not apply, the arbitrators may consider assessing interest at a rate appropriate to the currency of the award through the exercise of any discretion that they possess in determining damages under the governing substantive law or the arbitral law of the seat.

\textsuperscript{62} In the international context, particularly in the absence of an express provision in the parties’ contract, an arbitral tribunal may have discretion in determining the currency in which the award is rendered. See UNIDROIT PRINCIPLES Art. 7.4.12 (“Damages are to be assessed either in the currency in which the monetary obligation was expressed or in the currency in which the harm was suffered, whichever is more appropriate.”).

\textsuperscript{63} The 2012 U.S. Model Bilateral Investment Treaty recognizes the importance of matching the interest rate to the currency of the award. Article 6(3) of the Model Treaty provides that if the fair market value of an expropriated investment is denominated in a freely usable currency, the arbitral tribunal shall grant pre-award and post-award interest “at a commercially reasonable rate for that currency[.]” See also 2012 U.S. Model Bilateral Investment Treaty, Art. 6(4) (specifying compensation payable if fair market value of expropriated investment is denominated in currency that is not freely usable).

\textsuperscript{64} Pierre Mayer, Reflections on the International Arbitrator’s Duty to Apply the Law, 17(3) ARB. INT’L 235, 244 (2001). See also Secomb, supra note 6, at 440.
Alternatively, international arbitrators reasonably may conclude that the choice-of-law approach, holding that interest should be determined in accordance with the same law that governs liability and damages, is subject to an exception in an international case if the value of the currency of the governing law changes at a materially different rate from the value of the currency of the award. In such circumstances, the Committee believes that it would be appropriate for a tribunal to determine the entitlement to interest and the period during which interest accrues in accordance with the law governing the contract, while determining the interest rate, whether the interest is simple or compound, and (if it is compound) the compounding period in accordance with general principles of law. Such general principles include the prevailing party’s right to full compensation for the loss of use of money it was entitled to receive from the date when interest begins to accrue under the governing law until the date of the award. An international arbitration tribunal possesses discretion under general principles of law to assess

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65 Section 10 of the Restatement (Second) Conflict of Laws expressly recognizes that “[t]here may . . . be factors in a particular international case which call for a result different from that which would be reached in an interstate case.” The Reporters Notes to Section 10 of the Restatement observe that “[s]ome questions can arise only in international conflicts, [such] as questions involving . . . the conversion of one currency into another.”

66 This recommended choice-of-law rule is similar to the approach followed by the English courts, which determine liability to pay prejudgment interest in accordance with the law governing the merits, while determining the rate of interest in accordance with English law. See Dicey, Morris & Collins on the Conflict of Laws (15th ed.) § 7R-082, Rule 20(2). English law authorizes the High Court to award prejudgment interest on a simple-interest basis “at such rate as the court thinks fit[.]” Senior Courts Act, 1981, § 35A(1). In the exercise of its discretion under English law, the High Court “will, prima facie, award the rate applicable to the currency in which the debt is expressed.” Dicey, Morris & Collins, supra, § 7R-082, Rule 20(3) (footnotes omitted). See also, e.g., Miliangos v. George Frank (Textiles) Ltd., [1977] Q.B. 489, 497 (“while you look to the proper law of the contract to see whether there is a right to recover interest by way of damages, you look to the lex fori to decide how much”; court awarded damages in Swiss francs and held that claimant was entitled to prejudgment interest on a simple-interest basis “at a rate at which someone could reasonably have borrowed Swiss francs in Switzerland at simple interest”).

67 See UNIDROIT Principles Art. 7.4.10 (“Unless otherwise agreed, interest on damages for non-performance of non-monetary obligations accrues from the time of non-performance.”).
pre-award interest at a market rate appropriate to the currency of the award and on a compound basis. 68

Comment (e) to Section 823 of the Restatement (Third) of the Foreign Relations Law of the United States addresses the awarding of prejudgment interest by U.S. state and federal courts in international cases as follows:

The date for commencement of interest on an obligation or a judgment is determined by the law of the forum, including its rules on choice of law. When a statutory rate of interest is applicable in the forum, that rate must be applied, even if the judgment is given in foreign currency. If no statutory rate of interest is applicable, the court may, in appropriate cases, order interest to be based on the interest rate applicable at the principal financial center of the state issuing the currency in which the judgment is payable. 69

In accordance with the first sentence of this comment, read together with Comment (e) to Section 207 of the Restatement (Second) of Conflicts of Law, the law governing the merits of the parties’ dispute should determine the date for commencement of prejudgment interest. The second sentence appears to provide that a U.S. court must apply the forum’s statutory prejudgment interest rate, if any, in assessing prejudgment interest in an international case, “even if the judgment is given in foreign currency.” This approach to the applicable interest rate can

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68 See, e.g., UNIDROIT PRINCIPLES Art. 7.4.9(2) (providing that interest on late payments shall be payable at “the average bank short-term lending rate to prime borrowers prevailing for the currency of payment at the place for payment”); ICC Award No. 8769, ICC International Court of Arbitration Bulletin 10(2) (1999), at 75 (awarding interest at “commercially reasonable interest rate” in accordance with Article 7.4.9(2) of UNIDROIT Principles). International investment tribunals, applying international law, often assess pre-award interest at a market rate appropriate to the currency of the award and on a compound basis. A recent survey of pre-award interest determinations in 63 investment awards rendered between January 2000 and March 2016 found that 18 of the 63 awards surveyed (approximately 30%) assessed pre-award interest at a rate based on LIBOR, most often with an uplift of two percentage points. See Tiago Duarte-Silva & Jorge Mattamouros, Prejudgment interest – a mere afterthought?, 11(5) GLOBAL ARB. REV. 30, 31 (2016). LIBOR is a benchmark rate that the leading banks in London charge each other for short-term loans. Sixteen of the awards surveyed (25%) assessed interest at a rate not linked to any benchmark, most often from four to six percent, while nine of the awards (14%) assessed interest at a rate based on U.S. Treasury yields. Id. at 31-32. In the majority of recent awards, international investment tribunals have assessed interest on a compound basis. See RUDOLF DOLZER & CHRISTOPH SCHREUER, PRINCIPLES OF INTERNATIONAL INVESTMENT LAW 298 (2012).

give rise to anomalies for at least two reasons.\textsuperscript{70} First, if a statutory prejudgment interest rate is to be applied, the presumptively applicable interest rate in an international case generally is not the forum’s statutory rate, but the statutory rate under the governing substantive law.\textsuperscript{71} Second, a court or arbitral tribunal should consider the impact, if any, of the currency in which damages are to be awarded. If the value of the currency of the governing substantive law changes at a materially different rate than the value of the currency of the award, it may be inappropriate, as a general matter, for a court or arbitral tribunal to grant one of the parties a windfall by applying a statutory prejudgment interest rate that has no relevance to the loss incurred as a result of delay in recovery of compensation.\textsuperscript{72}

4. Law of the Arbitral Seat

The next step in the Committee’s suggested approach is for arbitrators to look to the law of the arbitral seat governing the arbitral process.\textsuperscript{73}

\textsuperscript{70} To the Committee’s knowledge, no U.S. court has ever cited or applied the second sentence of Comment (e) to Section 823 of the Restatement (Third) of the Foreign Relations Law of the United States. See, e.g., Amoco Cadiz, 954 F.2d at 1333 (“Rules for prejudgment interest . . . usually come from the law defining the elements of damages. . . . One would think, therefore, that prejudgment interest on the French plaintiffs’ claims depends on French law[.]”).

\textsuperscript{71} See RESTATEMENT (SECOND) OF THE CONFLICT OF LAWS § 207 cmt. e (1971).

\textsuperscript{72} In an article published in 1985, Professor Ronald Brand proposed that Section 823 of the draft Restatement (Third) of the Foreign Relations Law of the United States then under consideration be revised to include the following provision:

In giving judgment on a foreign currency obligation, a court may award both pre-judgment and post-judgment interest at such rate or rates as may be appropriate, taking into consideration the statutory rate of interest, if any, otherwise applicable and the rate of interest generally available in the market on investments made in terms of the currency in which judgment is made.

Ronald A. Brand, Restructuring the U.S. Approach to Judgments on Foreign Currency Liabilities: Building on the English Experience, 11(1) YALE J. INT’L L. 139, 184 (1985). As Professor Brand explained, this provision was “directed at the problem of matching the interest rate to the currency of judgment. Without such a rule, it is possible that a court would render judgment in one currency and apply the interest rate relevant to another currency[.]” Id. at 189. Professor Brand’s proposal was not adopted.

\textsuperscript{73} The choice of a seat almost invariably leads to the application of its arbitration law, and so parties should expect that their selection of a seat will affect numerous aspects of the arbitral process, potentially including the standards applicable to the awarding of interest. See, e.g., BORN, supra note 6, at 2052 (“[T]he law of the arbitral seat can directly govern a number of distinct legal issues affecting any international arbitration, many of which can be highly important.”). An arbitral tribunal, in considering an award of interest, may decide, in the face of evidence
As discussed in subsection (a) below, the law of the arbitral seat, when the seat is New York, accords with New York substantive law relating to the award of interest by international arbitrators. If, in a particular case, the law of the arbitral seat conflicts with the applicable substantive law relating to the award of interest by international arbitrators, the tribunal will need to determine how to reconcile the conflict. No such conflict exists when New York is the arbitral seat and New York substantive law governs the dispute. This Committee does not express a view as to how such conflicts might be addressed in arbitrations seated in other jurisdictions.

a. International Arbitrators’ Broad Remedial Powers Under Federal Arbitral Law

The Federal Arbitration Act and C.P.L.R. Article 75, New York’s arbitration statute, are silent with respect to the award of interest. It is well-settled, however, as a matter of federal and New York arbitral law that, “[w]here an arbitration clause is broad . . . arbitrators have the discretion to order remedies they determine appropriate, so long as they do not exceed the power granted to them by the contract itself.”

In the Committee’s view, the broad remedial powers of international arbitrators under federal arbitral law include at least the same discretionary power to award interest that the New York law allows. In a specific case that the contracting parties carefully considered the arbitration law of the seat, that the arbitration law of the seat be given greater weight in that case than the law governing the merits. However, contracting parties frequently select the seat of arbitration primarily or exclusively for reasons of logistical convenience and without regard to its arbitration law. Under the latter, more typical scenario in commercial cases, principles of party autonomy and respect for the intent of the parties arguably weigh in favor of giving the arbitration law of the seat lower priority than the law governing the merits of the parties’ dispute. Following the same logic, when parties neglect to designate the seat and, as a consequence, the seat is designated for the parties, arbitrators reasonably may decide not to give weight to the law of the seat as reflective in any way of party intent as to interest awards.

74 Banco de Seguros del Estado v. Mut. Marine Office, Inc., 344 F.3d 255, 262 (2d Cir. 2003) (federal law). See also, e.g., Benihana, Inc. v. Benihana of Tokyo, LLC, 784 F.3d 887, 902 (2d Cir. 2015) (“Like federal law, New York law gives arbitrators substantial power to fashion remedies that they believe will do justice between the parties and under New York law, arbitrators have power to fashion relief that a court might not properly grant.”) (internal quotation marks, ellipsis and citation omitted); Bd. of Educ. of Norwood-Norfolk Cent. Sch. Dist. v. Hess, 49 N.Y.2d 145, 152 (1979) (“[T]o achieve what the arbitration tribunal believes to be a just result, it may shape its remedies with a flexibility at least as unrestrained as that employed by a chancellor in equity.”); Silverman v. Benmor Coats, Inc., 61 N.Y.2d 299, 308 (1984) (arbitrator “may do justice as he sees it”); Benedict P. Morelli & Assocs., P.C. v. Shainwald, 854 N.Y.S2d 133, 134 (1st Dep’t 2008) (“Arbitrators are free to shape a remedy with unrestrained flexibility in order to achieve a just result.”).
York courts possess in equitable actions. In equitable actions, the New York courts enjoy discretion under C.P.L.R. Section 5001(a) to determine whether to award any interest and, if so, how much. As explained by the Appellate Division in *Rosenblum v. Aetna Casualty & Surety Co.*, 439 N.Y.S.2d 482 (3d Dep’t 1981),

> [I]t is . . . well settled that the inclusion of interest in recoveries in actions of an equitable nature is left to the sound discretion of the court (see CPLR 5001, subd [a]) and that arbitrators are empowered to fashion awards to achieve just results and may shape remedies with a flexibility at least as unrestrained as that employed by a chancellor in equity.

*Id.* at 483 (internal quotation marks, ellipsis and citation omitted). Although the underlying claim in *Rosenblum* was equitable, the Appellate Division’s conclusion that a tribunal’s broad remedial powers under New York law include the discretionary power to award interest applies equally regardless of whether the claim in the arbitration is characterized as legal or equitable.

An international arbitral tribunal seated in New York has discretion, therefore, to award such interest as it considers appropriate.

b. **International Arbitrators’ Power to Award Interest Under Other National Arbitration Laws**

The arbitration statutes of England and several predominantly British Commonwealth jurisdictions expressly grant to arbitral tribunals discretion to award such interest as they

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75 N.Y.C.P.L.R. § 5001(a) (“. . . in an action of an equitable nature, interest and the rate and date from which it shall be computed shall be in the court’s discretion”). By contrast, in actions of a legal nature, courts generally have no discretion under New York law with regard to prejudgment interest determinations. *See, e.g., United Bank*, 542 F.2d at 878 (“This Court has repeatedly held that since CPLR § 5001 is obviously phrased in mandatory terms, New York law does not permit the trial court to exercise any discretion with regard to prejudgment interest determinations.”).

76 *See Levin & Glasser*, 896 N.Y.S.2d at 312 (tribunal’s “broad authority to resolve disputes” includes power to award interest; nature of underlying claim in arbitration not specified); *West Side Lofts*, 751 N.Y.S.2d at 476 (arbitrator did not exceed his powers by granting pre-award interest; nature of underlying claim in arbitration not specified); *Grobman v. Chernoff*, No. 024250/98, 2008 N.Y. Misc. LEXIS 10792, at *3 (Sup. Ct. Nassau County 2008) (“an arbitrator’s power includes pre-award interest as part of a decision”; sole issue in arbitration was amount of damages owed for personal injuries).
consider appropriate. For example, Section 49(3) of the English Arbitration Act 1996 provides that “[t]he tribunal may award simple or compound interest from such dates, at such rates and with such rests as it considers meets the justice of the case . . . on the whole or part of any amount awarded by the tribunal[.]”

The House of Lords’ well-known decision in *Lesotho Highlands Development Authority v. Impregilo SpA*, [2005] UKHL 43, establishes that a tribunal seated in England has discretion to award interest under Section 49(3) of the English Arbitration Act even if the law governing the merits specifies how interest shall be calculated on damages. The dispute in that case arose under a contract governed by the law of Lesotho and providing for arbitration in London. The law of Lesotho included statutory interest provisions, but the tribunal disregarded those provisions in exercising its discretion to award interest under Section 49(3) of the Arbitration Act. The Court of Appeal held that the tribunal had exceeded its powers, reasoning that “there is no room for any discretionary procedural power” under Section 49(3) where the law governing the merits confers a substantive right to interest. The House of Lords reversed on the ground, *inter alia*, that Section 49 of the Arbitration Act allows an arbitral tribunal to award interest either by exercising its discretionary power under Section 49(3) or by applying the law governing the merits pursuant to Section 49(6).

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5. **General Guidelines for the Exercise of Discretion in Awarding Interest**

Federal case law with respect to the awarding of prejudgment interest by the federal district courts in federal question and admiralty cases may provide useful guidance for international arbitrators in the exercise of any discretion they possess with respect to the awarding of pre-award interest in arbitration, whether by virtue of the applicable arbitration rules, the applicable substantive law (or rules of law), or the applicable arbitration law. The federal district courts have broad discretion as to the awarding of prejudgment interest in such cases. Each Circuit has developed somewhat different guidelines for the exercise of this discretion. The Seventh Circuit Court of Appeals has set forth perhaps the clearest and most comprehensive set of guidelines. *See In re Oil Spill by the Amoco Cadiz*, 954 F.2d 1279, 1331-35 (7th Cir. 1992). In a *per curiam* opinion, Chief Judge Bauer and Judges Easterbrook and Fairchild set forth the following guidelines:

- A district court should award prejudgment interest at the market rate, because interest at this rate “puts both parties in the position they would have occupied had compensation been paid promptly.” *Id.* at 1331.

- The market rate is “the minimum appropriate rate for prejudgment interest, because the involuntary creditor [i.e., the prevailing party] might have charged more to make a loan.” *Id.*

- “Any market rate reflects three things: the social return on investment (that is, the amount necessary to bid money away from other productive uses), the expected change in the value of money during the term of the loan (i.e., anticipated inflation), and the risk of nonpayment. The best estimate of these three variables is the amount the defendant must pay for money, which reflects variables specific to that entity.” *Id.* at 1332.

- A district court need not try to determine the actual rate that the defendant must pay to borrow money. *Id.* If the court chooses not to engage in such “refined rate-setting,” it should award prejudgment interest at the U.S. prime rate, which is “the rate banks charge for short-term unsecured loans to credit-worthy...”

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customers.” *Id.* While the prime rate “may miss the mark for any particular party, . . . it is a market-based estimate.” *Id.*

- The relevant market rate is the rate in effect during the prejudgment period, “not the going rate at the end of the case.” *Id.* If the market rate fluctuated during the prejudgment period, the district court should calculate interest at the different rates in effect during this period. *Id.* at 1333. Alternatively, it may use an average rate during the period. *Id.* at 1335.

- The “norm” in federal litigation is to award prejudgment interest on a compound basis because (1) the defendant would have had to pay interest on unpaid interest if it had borrowed the amount of the damages and (2) the plaintiff could have earned interest on interest if it had invested or loaned that amount. *Id.* at 1331-32.

The Seventh Circuit’s guidelines are broadly similar to those developed by the other federal courts of appeals. For example, the Second Circuit held, in *Mentor Insurance Company (U.K.) Ltd. v. Norges Brannkasse*, 996 F.2d 506 (2d Cir. 1993), that the district court may award prejudgment interest at a rate that “reflects the cost of borrowing money, if measured for example by the average prime rate or adjusted prime rate[.]” *Id.* at 520. Judge Jacobs, writing for the panel, concluded that “[t]he award of compound interest . . . was within the district court’s broad discretion.” *Id.* Unlike the Seventh Circuit in *Amoco Cadiz*, the Second Circuit in *Mentor Insurance* held that (a) the district court may award interest at a short-term, risk-free rate, rather than the market rate, and (b) “a prevailing party is not entitled to a calculation of prejudgment interest at the interest rates at which it actually borrowed money during the period in question since consideration of the precise credit circumstances of the victim would inject a needless variable into these cases.” *Id.* (internal quotation marks and citation omitted).

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81 As of the date of this report (June 2017), the U.S. prime rate is 4.25%. If the tribunal assesses damages and issues its award in a currency other than the U.S. dollar, the Committee considers that it would generally be appropriate for it to use a market rate appropriate to the currency of the award. See subsection II.A.3.b supra.

82 See also, e.g., *Cont’l Transfert Technique Ltd. v. Fed. Gov’t of Nigeria*, 603 Fed. Appx. 1, 5 (D.C. Cir. 2015) (“This court has repeatedly concluded that the use of the prime rate in the award of prejudgment interest reflects an appropriate exercise of the district court’s discretion.”).
An arbitral tribunal may find guidance in judicial opinions that set forth guidelines intended to ensure that the prevailing party is fully compensated for its loss. Arbitral tribunals generally differ from most trial courts in being able to bring to bear whatever resources the parties consider appropriate in order to take into account the particular circumstances of the parties including, in appropriate cases, engaging in a “refined rate-setting” exercise. See Amoco Cadiz, 954 F.2d at 1332. In other cases they may choose to award interest at an appropriate market rate or at a risk-free rate. See Mentor Ins., 996 F.2d at 520.

Economists differ as to how pre-award (or prejudgment) interest should be calculated in order to compensate the prevailing party for the loss of use of money it was entitled to receive from the date its claim arose until the date of the award. For example, some economists espouse the “coerced loan” theory, which holds that pre-award interest should be calculated at the rate that the losing party would have paid a voluntary creditor because the losing party, by not immediately compensating the prevailing party for its harm, in effect forced the prevailing party to make a loan to the losing party equal in value to the prevailing party’s harm. Other economists argue that pre-award interest should be calculated at a rate equal to the prevailing party’s opportunity cost of capital. Several other approaches for determining the pre-award


84 See, e.g., Michael S. Knoll & Jeffrey M. Colon, The Calculation of Prejudgment Interest (2005), in PENN LAW: LEGAL SCHOLARSHIP REPOSITORY.

85 See, e.g., Manuel A. Abdala et al., Invalid Round Trips in Setting Pre-Judgment Interest in International Arbitration, 5(1) WORLD ARB. & MEDIATION REV. 1 (2011). In a number of industries and economic sectors, commercial enterprises have an opportunity cost of capital equal to or in excess of nine percent per annum. In those circumstances, at least, adoption of an “opportunity cost of capital” approach to calculating pre-award interest would tend to support the award of interest at New York’s nine percent statutory prejudgment interest rate as an appropriate estimate of the prevailing party’s opportunity cost of capital. On the other hand, a number of economists criticize the opportunity cost of capital approach to calculating pre-award interest on the ground, inter alia, that the prevailing party does not actually put any investment at risk; rather, the only risk that the prevailing party assumes is the risk that the losing party will not satisfy the award, and this risk may be compensated by requiring the losing party to pay interest at the rate that it would have paid a voluntary creditor. See, e.g., Dolgoff & Duarte-Silva, supra note 83 at 101 (“[T]here is an inconsistency introduced by applying ex ante cost of capital rates
interest rate also exist. It will generally be up to the parties in the arbitration to argue to the arbitral tribunal what rate is appropriate in the particular circumstances of their dispute.

The Seventh Circuit awarded the plaintiffs in the *Amoco Cadiz* case prejudgment interest at the average U.S. prime rate compounded annually, although it did not address the appropriate compounding period in its decision. It would not be inappropriate for arbitrators, in exercising their discretion, to award compound interest and to base the compounding period on factors specific to the parties and their industry.

Finally, the Committee believes that it is generally appropriate for pre-award interest to begin to accrue from the date of the non-performing party’s breach, except that interest upon damages incurred thereafter should generally begin to accrue from the date the damages were incurred. Subject to any countervailing equitable considerations, the awarding of interest until the date of the award generally appears to be necessary to provide full compensation to the prevailing party for the loss of use of its money.

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86 See Dolgoff & Duarte-Silva, *supra* note 83.


88 This pre-award period coincides with the periods specified in C.P.L.R. Section 5001(b) and UNIDROIT Principles Article 7.4.10. See N.Y.C.P.L.R. § 5001(b) (“Interest shall be computed from the earliest ascertainable date the cause of action existed, except that interest upon damages incurred thereafter shall be computed from the date incurred. Where such damages were incurred at various times, interest shall be computed upon each item from the date it was incurred or upon all of the damages from a single reasonable intermediate date.”); UNIDROIT PRINCIPLES Art. 7.4.10 (“Unless otherwise agreed, interest on damages for non-performance of non-monetary obligations accrues from the time of non-performance.”).
B. Post-Award, Prejudgment Interest

Parties sometimes request not only that arbitrators include pre-award interest as part of the total compensation due under the award, but also that the arbitral tribunal order the losing party to pay interest on the total amount of the award from the date the award is issued until the date it is paid. The Committee is also aware that there have been instances in which the ICC International Court of Arbitration, following its review of a tribunal’s draft award under Article 33 of the ICC Rules, has asked the tribunal to modify its award to address the granting of post-award interest, even if the prevailing party did not request such interest in its pleadings.

Increasingly, the practice is for arbitral tribunals to order the award-debtor to pay post-award interest if it does not satisfy the award within a specified time period. In U.S. courts, post-award interest ordered by an arbitral tribunal generally accrues from the date of the award (or the date on which payment is due under the award) until the date of a U.S. federal or state court judgment enforcing the award, even if the award provides that such interest shall accrue until the date the award is paid. Under the so-called merger doctrine, when an award is enforced through a U.S. federal or state court judgment, the debt created by the award merges with the judgment, such that the award debt is extinguished and, in the jurisdiction that rendered the judgment, only the judgment debt survives. Accordingly, “post-award” interest ordered by an arbitral tribunal comprises only post-award, prejudgment interest; post-judgment interest is separately determined in accordance with the law of the enforcement forum. In cases potentially involving enforcement proceedings in a forum that has not adopted a merger doctrine analogous to the

doctrine prevailing in the United States, there may be good practical reasons for the arbitral tribunal to award interest until the date the award is paid.

In the Committee’s view, it is generally appropriate for an arbitral tribunal to follow the same step-by-step methodology to identify the standards governing the award of post-award, prejudgment interest that an arbitral tribunal follows to determine the standards for pre-award interest. The fundamental guiding principles remain the same: respect for the intent of the parties and the compensatory purpose of interest. Not surprisingly, all of the arbitration rules that address the awarding of interest grant the arbitral tribunal discretion to award such pre-award and post-award interest as it considers appropriate.90

Accordingly, an arbitral tribunal, in exercising discretion with respect to post-award, prejudgment interest, may follow the guidelines set forth in subsection II.A.5 above for pre-award interest. Notwithstanding the arguably secondary purpose to encourage an award-debtor to satisfy an award promptly, the awarding of post-award, prejudgment interest at a rate higher than the rate of pre-award interest may be deemed an unenforceable penalty in some jurisdictions.91

C. Post-Judgment Interest

As noted above, “post-award” interest ordered by an arbitral tribunal only accrues until the date of a U.S. federal or state court judgment enforcing the award, because the debt created

90 See, e.g., ICDR International Arbitration Rules, Art. 31(4); LCIA Arbitration Rules, Art. 26.4; SIAC Arbitration Rules, Rule 32.9. One circumstance in which the governing standards for pre-award interest and post-award, prejudgment interest would differ is where the parties’ contract contains a clause specifically addressing the assessment of interest on any damages “until the date of award,” rather than “until the date of payment.”

91 See Laminioirs-Trefileries-Cableries de Lens, S.A. v. Southwire Co., 484 F. Supp. 1063, 1068-69 (N.D. Ga. 1980) (declining to enforce that portion of award assessing post-award interest at rates higher than rate of pre-award interest on ground that post-award rates were penal rather than compensatory). The Indian Arbitration and Conciliation Act (as amended in 2015) provides that, unless otherwise ordered by the arbitral tribunal, post-award interest shall accrue at a rate two percent higher than the Indian legal rate in effect on the date of the award. See INDIAN ARBITRATION AND CONCILIATION ACT 1996 § 31(7)(b).
by the award is deemed to merge into the judgment under the merger doctrine prevailing in the United States. Interest on the judgment, or “post-judgment interest,” is separately determined in accordance with the law of the enforcement forum. For U.S. federal court judgments, 28 U.S.C. Section 1961 specifies that interest shall be calculated from the date of entry of the judgment, “at a rate equal to the weekly average 1-year constant maturity Treasury yield . . . for the calendar week preceding the date of the judgment,” and that it shall be compounded annually.

It may be possible, under some circumstances, for parties to override the general merger rule and to specify a post-judgment interest rate, if the parties use “clear, unambiguous, and unequivocal” language indicating their intent that interest will accrue at this rate after the entry of a judgment. Contractual language stating that interest will accrue at a particular rate “until the principal is paid,” or other similar language, has been held not to meet this high standard.

Where the parties have agreed to a broad arbitration clause, the question whether they have sufficiently contracted for their own post-judgment rate is a determination reserved for the arbitral tribunal. Nevertheless, an award ordering that interest shall accrue at a particular rate “until the award is paid,” or other similar language, does not override the general rule on merger. Rather, the arbitral tribunal must use words that make crystal clear its intent to award interest in accordance with the law of the enforcement forum.

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92 See, e.g., Marine Mgmt., 574 N.Y.S.2d at 208; Westinghouse, 371 F.3d at 102; Tricon, 718 F.3d at 457; Fid. Fed. Bank, 387 F.3d at 1024.
94 Marine Mgmt., 574 N.Y.S.2d at 209; Westinghouse, 371 F.3d at 102; Tricon, 718 F.3d at 457; Fid. Fed. Bank, 387 F.3d at 1024.
95 Marine Mgmt., 574 N.Y.S.2d at 208-09; Tricon, 718 F.3d at 459.
96 Tricon, 718 F.3d at 457; Newmont, 615 F.3d at 1276-77.
97 Tricon, 718 F.3d at 459-60; Fid. Fed. Bank, 387 F.3d at 1022, 1024.
post-judgment interest.\textsuperscript{98} The Committee is aware of only one case in which an arbitral tribunal’s award was interpreted as awarding post-judgment interest.\textsuperscript{99}

International Commercial Disputes Committee
Richard L. Mattiaccio, Chair

\textit{June 2017}

\textsuperscript{98} \textit{Tricon}, 718 F.3d at 459-60.

\textsuperscript{99} \textit{See Newmont}, 615 F.3d at 1273, 1276-77 (tribunal’s award “provided for pre- and post-judgment interest at rate of 1.5\% per month”).
APPENDIX A

Arbitrators’ Pre-Award and Post-Award Interest Determinations in
International Commercial Arbitrations Governed by New York Substantive Law

<table>
<thead>
<tr>
<th>Arbitral Institution</th>
<th>Relevant Rules on Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>ICC</strong>: (International Chamber of Commerce)</td>
<td>The ICC Arbitration Rules are silent with regard to interest.</td>
</tr>
<tr>
<td><strong>ICDR</strong>: International Centre for Dispute Resolution</td>
<td>The ICDR International Arbitration Rules provide, at Article 31(4), that a tribunal “may award such pre-award and post-award interest, simple or compound, as it considers appropriate, taking into consideration the contract and applicable law(s).”</td>
</tr>
<tr>
<td><strong>IUSCT</strong>: Iran- U.S. Claims Tribunal</td>
<td>The IUSCT Arbitration Rules, which are adapted from the 1976 UNCITRAL Arbitration Rules, are silent regarding interest.</td>
</tr>
<tr>
<td><strong>LCIA</strong>: London Court of International Arbitration</td>
<td>The LCIA Rules provide, at Article 26.4, that “the arbitral tribunal may order that simple or compound interest shall be paid by any party on any sum awarded at such rates as the arbitral tribunal decides to be appropriate (without being bound by rates of interest practised by any state court or other legal authority).”</td>
</tr>
</tbody>
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<table>
<thead>
<tr>
<th>No.</th>
<th>Case</th>
<th>Case Details</th>
<th>Rate Applied</th>
<th>Approach to Interest</th>
</tr>
</thead>
</table>
- Seat: New York | 5% | The tribunal considered that a grant of pre-award interest was appropriate, and acknowledged that the CPLR rate was 9%. Nonetheless, the tribunal granted simple pre-award interest at a market rate. |
<table>
<thead>
<tr>
<th>No.</th>
<th>Case</th>
<th>Case Details</th>
<th>Rate Applied</th>
<th>Approach to Interest</th>
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<tbody>
<tr>
<td></td>
<td>(available via Westlaw Arbitration Materials)</td>
<td>- <strong>Law</strong>: New York</td>
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<td>rate of 5%, describing this rate as “market based.”</td>
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<td>- <strong>Year</strong>: 2007</td>
<td></td>
<td>The tribunal undertook a comparatively lengthy analysis of the applicability of the CPLR to pre-award interest. It concluded that while there was no doubt that New York law governed the contract at issue, “[t]his agreement by the parties does not extend to their joint agreement as to the applicability of Section 5004 of the Civil Practice Law and Rules (CPLR) of the State of New York.”</td>
</tr>
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<td>2</td>
<td>Grove Skanska v. Lockheed International A.G., ICC Case No. 3903 (excerpted in David J. Branson &amp; Richard E. Wallance, <em>Awarding Interest in International Commercial Arbitration: Establishing a Uniform Approach</em>, 28 Va. J. Int’l L. 919 (1987))</td>
<td>- <strong>Institution</strong>: ICC</td>
<td>Unspecified “realistic rate”</td>
<td>The contract at issue in this case provided that a party’s failure to make payments on time would carry the penalty of interest, but did not specify any particular interest rate. The contract had an unusual governing law clause which explicitly provided that “the law of the State of New York, U.S.A. (procedural and substantive) shall govern the interpretation of the Agreement.”</td>
</tr>
<tr>
<td></td>
<td></td>
<td>- <strong>Seat</strong>: Geneva</td>
<td></td>
<td>The prevailing party contended that interest should be computed at market rates (LIBOR +1%). LIBOR had been as high as 20% during the pre-award period. The losing party argued that interest should be set at the New York statutory prejudgment rate, which at that time was 6%.</td>
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<td>- <strong>Law</strong>: New York</td>
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<td>The tribunal first noted that, under New York case law, the question of interest is deemed substantive. However, the tribunal declined to apply the CPLR interest provisions on the ground that</td>
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| 3   | *Daum Global Holdings Corp. v. Ybrant Digital Ltd.*, ¶¶ 56–61 (available via Westlaw Arbitration Materials) | - **Institution:** ICC  
- **Seat:** Singapore  
- **Law:** New York  
- **Year:** 2013 | Unspecified | they only pertained to court actions and not to international arbitrations. The tribunal noted the “truly international flavor” of the dispute and stated that “in international commercial arbitrations it is generally accepted that arbitrators are entitled and indeed expected to award a realistic rate of interest.”  

The tribunal performed its own analysis of the CPLR, noting that the separate section dealing with arbitration (Article 75) does not cross-reference the CPLR prejudgment interest provisions, whereas it does explicitly refer to other portions of the CPLR such as the prescription rules found in Article 2. The tribunal stated that “[w]e approach §§ 5001 and 5004 on the footing that the rate of interest laid down may have the characteristic of a rule of practice to be applied in certain circumstances but not necessarily of universal application to all tribunals charged with the duty of deciding issues in accordance with the law of the State of New York.”  

The arbitrators conceded that if there was some indication that New York law was intended to limit interest rates in all contexts, it would control. Absent some clear indicia of such an intent, however, the tribunal did not believe that New York law had such a broad application.  

Ultimately, the tribunal granted interest at what it called a “realistic rate,” but did not give an indication of what it considered this to be. Instead, the tribunal expressed the hope and expectation that the parties would be able to agree on a mutually-acceptable, appropriate rate.  

In this case, the tribunal found that although New York law governed the merits of the parties’ dispute, interest was governed by Singapore law, as the lex arbitri. Section 20(1) of the Singapore Arbitration Act 2012 expressly grants to arbitral tribunals the authority to “award simple or compound interest from such date, at such rate and with such rest as the arbitral tribunal considers appropriate. . .”  

The tribunal further explained that CPLR Article 50 is “concerned
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| 4   | *NTT Docomo, Inc. v. Ultra D.O.O.* ¶ 85 (available via Westlaw Arbitration Materials) | - **Institution:** ICC  
- **Seat:** New York  
- **Law:** New York  
- **Year:** 2010 | U.S. Prime (3.25% - 4.25%) | The tribunal first noted that Docomo was entitled to pre-award and post-award interest at the New York statutory prejudgment interest rate pursuant to CPLR § 5001. However, it chose not to grant interest at this rate.  
Rather, the tribunal applied the U.S. Prime rate for pre-award interest, to run as of three separate dates for separate breaches. Similarly, the tribunal granted simple post-award interest at the Prime rate, to run until the award was paid or reduced to judgment.  
The tribunal did not provide a detailed explanation as to why it chose to apply the Prime rate over the New York statutory prejudgment interest rate. However, one factor that was likely relevant is that Docomo only claimed interest at the Prime rate, and Ultra made no submission in response. |
| 5   | ICC Case No. 10888 (excerpt available via ICC Dispute Resolution Library) | - **Institution:** ICC  
- **Seat:** Paris  
- **Law:** New York  
- **Year:** 2002 | U.S. Risk-Free | The tribunal had previously granted pre-award interest at a risk-free interest rate computed by an expert. Said interest was to run from the date of breach to the date of the award.  
Claimant applied for correction of the award, asserting that the tribunal should have awarded interest at the 9% New York statutory prejudgment interest rate.  
The tribunal rejected the application, noting that an international arbitral tribunal acting under the ICC Rules and seated in Paris was not bound to apply a rule on interest that was intended for the courts of New York State.  
The tribunal expressed concern that employing the New York rate would hinder the enforceability of its award, and instead chose the... |
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| 6   | *Al Maya Trading Establishment v. Global Export Marketing Co., Ltd.*, ¶ 88 (available via Westlaw Arbitration Materials) | - **Institution**: ICDR  
- **Seat**: New York  
- **Law**: New York  
- **Year**: 2016 | U.S. Prime Rate (3.25%) | “U.S. risk-free prejudgment interest rate,” which it viewed as more reflective of the economic reality.  
- The tribunal acknowledged that New York law prescribes 9%. However, it found that “in an international arbitration such as this, where the parties have not specifically agreed to any particular interest rate and no evidence was presented as to actual borrowing costs, we believe that the better course is to apply a commercial rate in the relevant currency.”  
- Notably, the tribunal cited to the *Grove Skanska* case in support of its proposition that “CPLR Article 50 . . . concerns court judgments.”  
- The tribunal thus granted pre-award interest at the U.S. Prime Rate. |
| 7   | *Butzel Long v. Valtech, S.A.*, ¶¶ 7.1–7.7 (available via Westlaw Arbitration Materials) | - **Institution**: ICDR  
- **Seat**: London  
- **Lex Arbitri**: England  
- **Law**: France, New York  
- **Year**: 2010 | 5% | The sole arbitrator concluded that interest was governed by the English Arbitration Act as the *lex arbitri*. Under Section 49 of that Act, an arbitral tribunal has broad discretion to fix the rate of interest.  
- The sole arbitrator granted pre-award interest at 5%, in accordance with English court practice. “This rate may be in excess of the interest rate at which Valtech could borrow from a bank,” it was “designed to encourage Valtech to resist the temptation to delay payment to Chesapeake of the sums due it, in effect using Chesapeake as its de facto banker.” For post-award interest, the Arbitrator similarly applied a rate of 5% both for damages and costs, with a three-week grace period for the latter. This interest was to be compounded quarterly. |
- **Seat**: The Hague  
- **Law**: New York  
- **Year**: 1986 | 10% | In this case, the tribunal applied LIBOR +3% for damages relating to most of the contractual breaches found. For one breach, the tribunal applied a 10% rate, deeming this “reasonable.”  
- Notably, neither party argued for the application of the New York statutory prejudgment interest rate, even though New York law |
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- Seat: New York  
- Law: New York  
- Year: 2016 | 8% | The parties’ contract (an attorney-client fee agreement) provided that the client could elect to make certain payments due under the contract over a period of 10 calendar quarters at an annual interest rate of 8%. The tribunal held that this provision was not directly applicable to the amount due by the client and considered the contract ambiguous as to whether the parties intended the 8% contractual rate or the 9% statutory rate to apply to this amount. The tribunal rejected the law firm’s request for 9% pre-award interest, noting that “[u]nder New York law, where a contract provides that interest will be paid at a specific rate until the principal has been paid, the contract rate governs, not the statutory rate, and interest is due until payment of the principal is made or until the contract is merged into a judgment.” The tribunal further noted that “[a]mbiguous provisions in attorney-client fee agreements are to be construed in a manner most favorable to the client.” |
- Seat: New York  
- Law: New York, Venezuela  
- Year: 2014 | Default Rate (4.875%) | The relevant contract in this case was unusual, in that it provided for an interest rate that was specifically to be applied to damages. It read, in relevant part: “[S]eller Damages] shall bear interest at the Default Rate pursuant to Section 4.2 from such Damages Due Date until the date of payment.” The tribunal had previously rendered a Partial Award in which it awarded respondent Seller Damages under the contract. The parties had agreed that pre-award interest should be granted at the Default Rate (4.875%), and that it should run from the date when Seller Damages became due until the date of the Partial Award. Respondents sought the 9% statutory prejudgment interest rate for |
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- Seat: New York  
- Law: New York  
- Year: 2014 | 10% | post-award interest, arguing that the contract did not specify a rate for post-award interest. The tribunal held that this provision was tantamount to a post-award interest provision, given that it specified that interest was to run “until the date of payment.” The tribunal thus awarded post-award interest at the Default Rate of 4.875%, reasoning that applying the New York statutory prejudgment interest rate would be contrary to the parties’ agreement. The tribunal construed the term “Requirements of Law” as addressing only those laws that set upper limits on interest, such as usury statutes. To hold otherwise, the tribunal reasoned, would be to needlessly abridge the parties’ freedom to contractually agree on an interest rate of their choice. The tribunal further concluded that the interest rates specified under the contract were not prohibited by New York’s anti-usury laws. As such, the tribunal granted simple pre-award interest at 8% up until the “default date,” and 10% interest thereafter. The tribunal also granted simple post-award interest at 10%. |
| 12  | *CIMC Raffles Offshore Ltd. v. Schahin Holdings, S.A.*, ¶ 81(1)(a)-(c) (available via Westlaw Arbitration Materials) | - Institution: ICDR  
- Seat: New York  
- Law: New York (?)  
- Year: 2012 | LIBOR +2% | The contract included an interest rate of LIBOR +2%. The tribunal granted pre-award interest at the contractual rate. However, the tribunal granted post-award interest at the statutory 9% rate, which was to run beginning 30 days after the rendering of the award. The tribunal did not explain why it decided to apply different rates |
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- Seat: New York  
- Law: New York  
- Year: 2012 | EURIBOR + 400 basis points | The contract stipulated an interest rate of EURIBOR + 400 basis points for late payments.  
The tribunal granted pre-award interest at the contractual EURIBOR rate. For post-award interest, the tribunal awarded 5% simple interest to run on unpaid amounts beginning 30 days from the issuance of the award until payment in full. The tribunal noted that this 5% rate corresponded closely to the rate that the parties agreed to in the contract (EURIBOR +400 basis points). |
| 14  | *Amaprop Ltd. v. Indiabulls Financial Services Ltd.*, ¶¶ 155–56 (available via Westlaw Arbitration Materials) | - Institution: ICDR  
- Seat: New York  
- Law: New York, India  
- Year: 2011 | 12% | The agreement between the parties provided that the respondent would pay 12% interest per annum on all amounts borrowed.  
The tribunal, invoking the contract as well as equitable considerations and arbitral practice, awarded pre-award and post-award interest at the 12% contractual rate. |
| 15  | *Agrera Investments, Ltd. v. Palant*, ¶ 68 (available via Westlaw Arbitration Materials) | - Institution: ICDR  
- Seat: New York  
- Law: New York  
- Year: 2011 | 12% | The contract provided for a 12% interest rate on payments for purchase of shares, pursuant to a contractual stock purchase option.  
The tribunal applied the contractual rate, in light of the fact that claimant sought damages for breach of the very contractual provision that provided for the 12% interest rate. |
- Seat: New York  
- Law: New York  
- Year: 2010 | 12% | The tribunal granted pre-award interest on damages as well as on the fees and costs awarded. The tribunal did not specify the interest rate it was applying, although claimant had requested interest at the contractual rate applicable to late payments (12%). |
| 17  | *KWV Int’l (Pty) Ltd. v. Peter Andrew LLC*, pp. 12–13 | - Institution: ICDR | 7% | One of the contracts at issue provided for an interest rate of 7% on overdue payments; the other was silent on interest. |
Despite the fact that “[b]oth parties have requested pre and post award interest at the New York statutory rate of 9% per annum,” the sole arbitrator concluded that the contractual interest provision reflected what the parties had deemed an appropriate rate of interest for their business arrangement and accordingly awarded interest at the 7% contractual interest rate, to run from the date of breach until the date of payment.

In arbitrations where the contract between the parties was silent on the issue of interest, arbitral tribunals have often granted pre-award and/or post-award interest at the 9% New York statutory prejudgment interest rate. Those tribunals that have issued (often perfunctory) reasoned decisions on this issue have generally relied on the parties’ choice of New York law as the law governing the contract.

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<td>18</td>
<td>Organizacion Ideal, S. de R.L. de C.V. v. FHR Mexico Management Company, S.A. de C.V., ¶¶ 484–500</td>
<td>Institution: AAA&lt;br&gt;- Seat: New York&lt;br&gt;- Law: New York&lt;br&gt;- Year: 2017</td>
<td>The sole arbitrator granted pre-award interest at the 9% statutory rate. In this case, the parties apparently agreed that CPLR §§ 5001 and 5004 governed the grant of interest. The dispute related solely to whether the grant of pre-award interest on an award of lost profits would constitute double recovery and a windfall for the award creditor. The sole arbitrator considered that New York law did not bar the grant of prejudgment interest on lost profits.</td>
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<td>19</td>
<td>Digitelcom Ltd. v. Tele2 Sverige AB, ¶ 457</td>
<td>Institution: ICDR&lt;br&gt;- Seat: New York&lt;br&gt;- Law: New York&lt;br&gt;- Year: 2011</td>
<td>The tribunal granted post-award interest on costs, to run beginning 15 days from the rendering of the award. It applied the New York 9% statutory prejudgment interest rate, holding that it was appropriate given that New York law governed the contract and New York was the seat of arbitration.</td>
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<td>20</td>
<td>Kailuan Int’l Co., Ltd v. Sino East Minerals Ltd, ¶¶ 136–37</td>
<td>Institution: ICC&lt;br&gt;- Seat: New York</td>
<td>The tribunal, citing the CPLR, granted pre-award interest at the statutory 9% rate, stating that “[w]e find this rate appropriate” because New York law governed the contract. The tribunal further granted post-award interest at 9%, to run beginning 30</td>
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| 21  | Logic, S.P.A. v. L-3 Communications Corp., ¶ 111 (available via Westlaw Arbitration Materials) | - **Institution:** ICC  
- **Seat:** New York  
- **Law:** New York  
- **Year:** 2015 | This decision is notable in that the tribunal explicitly found that it was not bound to apply the New York statutory prejudgment interest rate. However, citing to CPLR §§ 5001 and 5004, it found the 9% rate “appropriate” because it was the rate applied to New York court judgments and therefore “may be used by arbitral tribunals for guidance.”  
The tribunal granted simple pre-award interest at 9%, running from the date of breach. It also granted 9% post-award interest until the date the award was paid. |
| 22  | Sexton v. Karam et al., ¶¶ 218–222 (available via Westlaw Arbitration Materials) | - **Institution:** ICDR  
- **Seat:** New York  
- **Law:** New York  
- **Year:** 2014 | The tribunal did not grant pre-award interest, as it had rejected the claimant’s claims and there were no counterclaims. However, it did grant post-award interest on its award of costs and fees.  
The tribunal noted that Article 28(4) of the ICDR Rules allowed it to “award such . . . post-award interest . . . as it considers appropriate, taking into consideration the contract and applicable law.”  
The tribunal further indicated that the “New York CPLR does not set forth a post-award interest rate for international arbitrations seated in New York and does not mandate the application of its post-judgment interest rate to such arbitrations. Further, it is generally accepted in international arbitration that neither the statutory post-judgment interest rate at the seat of arbitration nor the statutory post-judgment interest rate of the law governing the contract mandatorily applies. Instead, arbitrators generally have wide discretion to determine the applicable interest rate, and the ICDR Rules reflect this principle.”  
In exercise of its discretion, the tribunal nonetheless chose to apply the 9% CPLR rate “that would apply to a judgment rendered by a New York state court as of the date of this Final Award.” |
| 23  | Barracuda and Caratinga Leasing Co., B.V. v. Kellogg Brown & Root, LLC, at Part K(A) (available via Westlaw Arbitration) | - **Institution:** LCIA  
(UNCITRAL Rules)  
- **Seat:** New York | This arbitration, while administered by the LCIA, was conducted pursuant to the 1976 UNCITRAL Arbitration Rules, which are silent as to the award of interest.  
The tribunal declined to grant any pre-award interest, noting that the claimant did not request such interest and that the claimant had not incurred additional replacement costs.
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- Year: 2011 | costs that would warrant the grant of pre-award interest.  
With respect to post-award interest, the tribunal granted the New York statutory prejudgment interest rate because New York law was the “law applicable to the arbitration” and the contract. This post-award interest was applied both to damages and to the costs awarded by the tribunal. |
| 24  | *Aconcagua Investing Ltd. v. Ingaseosas International Co.*, ¶¶ 165–66 (available via Westlaw Arbitration Materials) | - Institution: ICDR  
- Seat: Miami  
- Law: New York  
- Year: 2008 | The sole arbitrator granted pre- and post-award interest at the 9% statutory prejudgment interest rate, reasoning that “no interest rate was stipulated” in the contract.  
The sole arbitrator determined that pre-award statutory interest would run from the date of breach as determined by the arbitrator. Post-award interest would begin accruing if payment of the amount awarded was not made within 30 days. |

**Awards Granting Interest at the New York Statutory Prejudgment Interest Rate (Unreasoned Decisions)**

Many awards that have granted interest at the 9% statutory prejudgment interest rate have done so without any analysis.

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- Seat: New York  
- Law: New York  
- Year: 2016 | The sole arbitrator granted 9% pre-award interest pursuant to CPLR §§ 5001 and 5004. The sole arbitrator did not provide any reason for this award other than that the claimant was “entitled” to statutory interest. |
| 26  | *Moses & Singer LLP v. Cleveland Heart, Inc.*, ¶ 1–7 (available via Westlaw Arbitration Materials) | - Institution: AAA  
- Seat: New York  
- Law: New York  
- Year: 2015 | The sole arbitrator granted 9% interest pursuant to CPLR § 5004 to each of seven sums due under seven separate invoices. |
| 27  | *Travelers v. Idas Celik Enerji Tersane ve Ulaşım Sanayi A.S.* (available via Westlaw Arbitration Materials) | - Institution: ICDR  
- Seat: New York  
- Law: New York | For pre-award interest, the tribunal simply awarded a lump sum amount. For post-award interest, the tribunal granted interest at the New York statutory prejudgment interest rate to run on any amounts unpaid within 30 days of issuance of the arbitral award. |
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| 28  | *Hard Way, LLC v. Roc Fashions, LLC*, p. 2 (available via Westlaw Arbitration Materials) | - **Institution**: ICDR  
- **Seat**: New York  
- **Law**: New York  
- **Year**: 2014 | The tribunal granted a fixed figure for pre-award interest ($68,219.18 interest through June 18, 2014 plus $4.28 per day through date of award). For post-award interest, the tribunal granted 9% statutory interest, to run beginning 30 days after the rendering of the award. |
| 29  | *Caldera Resources, Inc. v. Global Gold Mining, LLC*, ICDR Case No. 50 2010 00674, p. 40 (available via Westlaw Arbitration Materials) | - **Institution**: ICDR  
- **Seat**: New York  
- **Law**: New York (?)  
- **Year**: 2014 | The tribunal neither granted nor discussed pre-award interest. It granted post-award interest at New York’s statutory prejudgment interest rate of 9% on most categories of damages awarded, running from the date of award. |
| 30  | *Garcia v. Ridge C.C.*, ¶¶ 66, 82 (available via Westlaw Arbitration Materials) | - **Institution**: ICC  
- **Seat**: New York  
- **Law**: New York  
- **Year**: 2014 | The tribunal granted 9% simple pre-award and post-award interest. The pre-award interest was to run from the date of breach. The tribunal opted to grant simple interest despite a contractual provision that allowed it discretion to grant compound interest. |
| 31  | *Schulte, Roth & Zabel, LLP v. China North Docl East Petroleum Holdings Ltd.*, p. 8 (available via Westlaw Arbitration Materials) | - **Institution**: ICDR  
- **Seat**: New York  
- **Law**: New York (?)  
- **Year**: 2014 | The sole arbitrator granted pre-award interest at the 9% statutory prejudgment interest rate, to run from date of breach. There was no discussion of post-award interest. |
- **Seat**: New York  
- **Law**: New York  
- **Year**: 2014 | The sole arbitrator referenced the contractual choice of New York law and noted that “under New York law, interest is normally allowed and awarded as a matter of course.” He granted pre-award interest at 9%. He also granted post-award interest at the statutory prejudgment interest rate. |
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<td>33</td>
<td>CE Int’l Resources Hldgs, LLC v. S.A. Minerals Ltd. Partnership, ¶ 75 (available via Westlaw Arbitration Materials)</td>
<td>Institution: ICDR - Seat: New York - Law: New York - Year: 2013</td>
<td>The sole arbitrator granted 9% statutory interest, to run from the approximate date of breach. This interest was to run until award-debtor received payment in full.</td>
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<td>34</td>
<td>Toshiba Corp. v. Nat’l Film Laboratories, Inc. (available via Westlaw Arbitration Materials)</td>
<td>Institution: ICDR - Seat: New York - Law: New York - Year: 2012</td>
<td>The sole arbitrator granted post-award interest at the statutory prejudgment interest rate on attorney’s fees and costs, to begin running immediately after the rendering of the award. There was no mention of pre-award interest.</td>
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<td>35</td>
<td>Colt Int’l Ltd. v. Altpower, Inc. (available via Westlaw Arbitration Materials)</td>
<td>Institution: ICDR - Seat: New York - Law: New York - Year: 2012</td>
<td>The sole arbitrator granted pre-award interest at the statutory prejudgment interest rate, to run from a date fixed after the commencement of the arbitration. There was no mention of post-award interest.</td>
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<td>37</td>
<td>Amri Rensselaer, Inc. v. Borregaard Industries Ltd., ¶ 3 (available via Westlaw Arbitration Materials)</td>
<td>Institution: ICDR - Seat: New York - Law: New York - Year: 2010</td>
<td>The sole arbitrator cited to the CPLR, and granted pre-award interest at the statutory prejudgment interest rate. The interest was to run from the date on which claimant received notice of the termination of the contract at issue. The sole arbitrator also granted post-award statutory interest at 9%, to run until date of payment.</td>
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<tr>
<td>38</td>
<td>A.G.k. SARL v. A.M. Todd Co., ¶ 17 (available via Westlaw Arbitration)</td>
<td>Institution: ICDR</td>
<td>The tribunal granted pre-award interest at the 9% statutory prejudgment interest rate. The interest was to run from the date the arbitration commenced, given the extreme</td>
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<td>39</td>
<td>Lizton Trading, Ltd. v. ATM Lenders, LLC, ¶¶ 190–91, 194 (available via Westlaw Arbitration Materials)</td>
<td>- <strong>Institution</strong>: LCIA  - <strong>Seat</strong>: London  - <strong>Law</strong>: New York  - <strong>Year</strong>: 2008</td>
<td>With respect to pre-award interest, the tribunal stated that it would exercise “its discretion to apply the New York rate of interest of 9% to the principal sums awarded.” This was to be a simple interest rate, running from the date of breach. Similarly, for post-award interest, the tribunal granted simple interest at New York’s statutory prejudgment interest rate. This was uncontested. The tribunal awarded interest at a rate of LIBOR +2% on the costs of the arbitration if not paid within 14 days.</td>
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<td>40</td>
<td>Navneet Publications India Ltd. v. American Scholar, Inc., ¶¶ 5.2-5.3 (available via Westlaw Arbitration Materials)</td>
<td>- <strong>Institution</strong>: ICDR  - <strong>Seat</strong>: New York  - <strong>Law</strong>: Unclear  - <strong>Year</strong>: 2008</td>
<td>The sole arbitrator granted the claimant 9% pre-award interest running from the date of breach, and 9% post-award interest on any unpaid amounts to begin running 30 days from the date the award was rendered.</td>
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<td>41</td>
<td>Colonial Oil Industries, Inc. v. Masefield America, Inc., ¶ 5.3 (available via Westlaw Arbitration Materials)</td>
<td>- <strong>Institution</strong>: ICC  - <strong>Seat</strong>: New York  - <strong>Law</strong>: New York  - <strong>Year</strong>: 2007</td>
<td>The tribunal granted both pre-award and post-award interest at the 9% statutory prejudgment interest rate.</td>
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<td>42</td>
<td>Lubiam Modo per l’Uomo SPA v. Chesa Int’l Ltd., ¶ 19 (available via Westlaw Arbitration Materials)</td>
<td>- <strong>Institution</strong>: ICDR  - <strong>Seat</strong>: New York  - <strong>Law</strong>: New York  - <strong>Year</strong>: 2007</td>
<td>The tribunal granted pre-award interest “at the legal rate of interest permitted under the law of New York.” The interest was to run until the date of payment.</td>
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<td>43</td>
<td>Esso Exploration and Prod. Chad Inc. v.</td>
<td>- <strong>Institution</strong>: ICC</td>
<td>In this case, the applicability of the 9% statutory prejudgment interest rate was uncontested. The sole arbitrator granted pre-award interest, to run from “an</td>
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|     | *Taylors Int’l Svcs. Ltd.*, ¶¶ 58, 60 (available via Westlaw Arbitration Materials) | - **Seat**: New York  
- **Law**: New York  
- **Year**: 2006 | appropriate midpoint of the various dates on which Esso Chad incurred the losses suffered by it.”  
Post-award interest at the 9% rate was granted on both damages and the costs and fees awarded by the tribunal. It was to run starting 1 month and 1 week after the rendering of the award. |
| 44  | *Capital India Power Mauritius I v. Maharashtra Power Dev’t Corp. Ltd.*, ICC Award No. 12913/MS, pp. 34–36 (available via italaw.com) | - **Institution**: ICC  
- **Seat**: New York  
- **Law**: New York  
- **Year**: 2005 | The tribunal granted 9% simple pre-award interest, to run from the date of the destruction of claimant’s equity in an investment project in breach of a Shareholders Agreement. The tribunal invoked its discretion to decline to grant pre-award interest on arbitration costs.  
The tribunal also granted 9% simple post-award interest. |
| 45  | *Chemical Overseas Hldgs, Inc. v. Uruguay*, ¶¶ 64–65, 68(a) and 68(h) (available via Westlaw Arbitration Materials) | - **Institution**: ICC  
- **Seat**: New York  
- **Law**: New York  
- **Year**: 2004 | Invoking the CPLR, the tribunal held that claimants were entitled to simple 9% interest “from the earliest ascertainable date the cause of action existed.”  
The tribunal also granted simple post-award interest at the statutory 9% rate. |
| 46  | *ICC Case No. 9839*, ¶ 63 (excerpt available in 2004 Y.B. Com. Arb. 66) | - **Institution**: ICC  
- **Seat**: Unclear  
- **Law**: New York  
- **Year**: 1999 | The tribunal held that, under CPLR § 5001, the petitioner was owed 9% interest from the earliest possible date its cause of action existed. This 9% interest was to run until petitioner received full payment of the sum awarded. |
- **Seat**: The Hague  
- **Law**: Unclear  
- **Year**: 1982 | In this case, a check issued by the respondent to claimant remained unpaid due to a presidential order of 14 November 1979, freezing respondent’s U.S. assets. A consent judgment was filed in the New York Count Clerk’s office on 28 February 1980.  
Before the Iran-U.S. Claims Tribunal, the claimant sought the principal amount of this judgment plus interest running from 14 November 1979. For its part, the respondent claimed that no interest should be payable on the principal amount because its funds in the U.S. were frozen.  
The tribunal noted evidence that respondent’s U.S. funds had yielded interest during the period in question, and therefore respondent could not be exempted from paying New York statutory interest. |
The tribunal applied §§ 5003 and 5004 of the CPLR in its analysis. The application of § 5003, which deals with post-judgment interest, was a product of the unusual circumstances of this case, *i.e.* that the tribunal was dealing with an award that followed a New York state court judgment.

The tribunal granted pre-award interest at 6% up to and including 24 June 1981. After that date, pre-award interest was raised to 9% to match the increase in the CPLR rate. This interest was to run from the date of the consent judgment.

No post-award interest was granted.
# APPENDIX B

New York Federal and State Court Decisions Reviewing Arbitrators’ Awards of Interest

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<th>No.</th>
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<td><strong>Federal Court Decisions Reviewing Arbitrators’ Interest Awards</strong></td>
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<td>1</td>
<td><em>Waterside Ocean Navigation Co. v. International Navigation Ltd.</em>, 737 F.2d 150 (2d Cir. 1984)</td>
<td>In this New York Convention case, the lower court had confirmed the tribunal’s award without granting post-award, prejudgment interest, stating that it did not have jurisdiction to “go beyond confirmation” of the award. On appeal, the Second Circuit held that whether to grant post-award, prejudgment interest in cases arising under federal law has, in absence of statutory directive, been placed in the “sound discretion” of the district courts. The court noted that there is a presumption in favor of the award of prejudgment interest, and that the facts did not indicate that award of prejudgment interest would be inappropriate in this case. The case was thus remanded to the district court for computation of post-award, prejudgment interest at a “appropriate rate.”</td>
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<td>2</td>
<td><em>Manios v. Zachariou</em>, No. 14CV4331-LTS-DCF, 2015 U.S. Dist. LEXIS 42537 (S.D.N.Y. 2015)</td>
<td>In this proceeding to vacate an international arbitral award under Chapter 2 of the Federal Arbitration Act (“FAA”), the award-creditor argued that the arbitrators had manifestly disregarded the law by granting pre-award interest on a distribution of assets in an estate settlement case. The award-creditor contended that the terms of CPLR § 5001 only allow for interest upon “a sum awarded.” The court rejected the award-creditor’s “manifest disregard” claim, holding that where parties agree to submit a dispute to AAA arbitration (such as in the instant case), the AAA Commercial Rules are incorporated into the underlying agreement. Because the AAA Rules grant arbitrators the authority to award interest at such rate and from such date as they may deem appropriate, the tribunal did not manifestly exceed its authority by granting pre-award interest in this case. Accordingly, the award-debtor was not entitled to vacatur of the arbitral tribunal’s award under the FAA.</td>
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<td>3</td>
<td><em>Sayigh v. Pier 59 Studios</em>, No. 11-CV-1453-RA, 2015 U.S. Dist. LEXIS 27139, at *37 (S.D.N.Y.</td>
<td>In this proceeding to modify or vacate an arbitral award, the award-creditor argued that the arbitrator manifestly disregarded New York law by not granting her pre-award interest.</td>
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<td>Mar. 5, 2015)</td>
<td>The court rejected this argument, first noting that CPLR § 5001 (providing that interest shall be recovered on a sum awarded for breach of contract) was inapplicable, as the underlying dispute concerned an alleged act of employment discrimination. The court further held that, “where an arbitrator could have awarded pre-award prejudgment interest but did not, the court may not do so when entering judgment on an arbitration award.” The court, applying CPLR § 5002, granted “post-award prejudgment interest at an annual rate of 9%” as well as post-judgment interest at the rate provided for in 28 U.S.C. § 1961(a).</td>
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<td>4</td>
<td><em>Local Union No. 1 of the United Assn. of Journeymen &amp; Apprentices of the Plumbing &amp; Pipe Fitting Indus. v. Bass Plumbing &amp; Heating Corp.</em>, 2014 U.S. Dist. LEXIS 183085 (E.D.N.Y. Oct. 28, 2014)</td>
<td>In this proceeding to confirm a domestic arbitral award, the arbitral tribunal had not granted post-award, prejudgment interest. Petitioner sought, along with confirmation of its award, to obtain interest from the date of the award. Magistrate judge Viktor Pohorelsky found that where an award is silent as to prejudgment interest, a court is not entitled to award such interest. He therefore recommended that Petitioner’s request for interest be denied. This recommendation was adopted, and a judgment was entered in <em>Local Union No. 1 of the United Assn. of Journeymen &amp; Apprentices of the Plumbing &amp; Pipe Fitting Indus. v. Bass Plumbing &amp; Heating Corp.</em>, 2015 U.S. Dist. LEXIS 37932 (E.D.N.Y. Mar. 25, 2015). This judgment is at odds with the weight of New York federal case law, which provides that courts have discretion to grant post-award, prejudgment interest where the arbitral award is silent as to such interest. The outcome of this case appears to have resulted from the Magistrate Judge’s misreading of certain precedents (<em>see Shamah v. Schweiger and Moran v. Arcano</em>, below) which had referred to pre-award interest as “prejudgment” interest.</td>
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<td><em>PremiereTrade Forex, LLC v. FXDirectDealer, LLC</em>, No. 12 CIV. 7006 PAC, 2013 WL 2111286 (S.D.N.Y. May 16, 2013)</td>
<td>In this proceeding to confirm a domestic arbitral award, the tribunal in the underlying arbitration had granted post-award interest at the New York statutory prejudgment interest rate of 9%, to begin running 30 days after the award. During the confirmation proceeding, the award-creditor sought a separate, additional award of prejudgment interest at 9% per annum, on top of the arbitrators’ award of post-award interest. The court denied the award-creditor’s request for duplicative post-award, prejudgment interest, noting that “confirmation of the award will include post-award interest at a rate of 9% specified in the arbitrators’ opinion”. The court further noted that, to the extent the award-creditor’s request for prejudgment interest referred to pre-award interest, “the Court will not grant interest that the arbitrators in this action explicitly denied.”</td>
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<td><em>Ganfer &amp; Shore, LLP v. Witham</em>, 2011 U.S. Dist. LEXIS 2622 (S.D.N.Y. 2011)</td>
<td>In this proceeding to confirm a domestic arbitral award, the court held that where an arbitral tribunal does not grant pre-award interest, a court cannot award such interest on a motion to confirm the arbitration award. By contrast, the court held that it was required to grant post-award, prejudgment interest “absent circumstances warranting the contrary” and that post-judgment interest was similarly “mandatory.”</td>
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<td><em>Finger Lakes Bottling Co. v. Coors Brewing Co.</em>, 748 F.Supp.2d 286, 292-93 (S.D.N.Y. 2010)</td>
<td>In this proceeding to confirm a domestic arbitral award, the court first noted that, where arbitrators have authority to grant pre-award interest, courts cannot grant such interest in post-award proceedings. However, in this case the issue of interest was beyond the scope of the parties’ narrowly-worded and limited arbitration agreement. New York law governed the granting of pre-award interest, because this was a diversity case and New York law governed the arbitration agreement. The award-creditor was not entitled to interest at the 9% statutory prejudgment interest rate because it did not assert a claim for breach of contract. Rather, because the proceeding was one of an equitable nature, the court had discretion to grant pre-award interest under CPLR § 5001. The court ultimately granted interest at the treasury bill rate, reasoning that the New York statutory prejudgment interest rate was not in line with actual market conditions.</td>
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<td>8</td>
<td><em>Petrie v. Clark Moving &amp; Storage, Inc.</em>, No. 09-CV-06495, 2010 U.S. Dist. LEXIS 48460 (W.D.N.Y. 2010)</td>
<td>In this proceeding to confirm a domestic arbitral award, the award-creditor requested that the court grant pre-award interest at the 9% rate specified in CPLR § 5004. The court rejected the award-creditor’s claim, noting that arbitrators may provide for pre-award interest as part of their award, but if the award is silent on pre-award interest courts may not grant it. Because the “court is not entitled to award an amount relating to such prejudgment interest . . . the parties must determine the applicable interest rate and calculate the amount due.”</td>
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| 9   | *Coastal Caisson Corp. v. E.E. Cruz/NAB/Frontier-Kemper*, 2007 U.S. Dist. LEXIS 58114 (S.D.N.Y. Aug. 10, 2007) | In this proceeding to confirm a domestic arbitral award, the award-creditor moved to modify the award to add prejudgment interest. The award-creditor sought 9% prejudgment interest pursuant to the CPLR, from the date the contract balance was due. The arbitral tribunal held that “[a]lthough prejudgment interest may be required by the CPLR, we find that we have discretion under the applicable rules of the American Arbitration Association not to award pre-award interest . . . . Given the vast uncertainties concerning the amounts due and the reasons for those uncertainties . . . . we think it is highly inappropriate to award interest and we decline to do so.” In denying the award-creditor’s motion to modify the award, the court noted that “the arbitrators did not
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<td>The court noted that the parties had selected the American Arbitration Association Construction Industry Rules and New York law to govern their dispute. The former, at Rule 44(d), grant arbitrators discretion to award such interest as they may deem appropriate. The latter, at CPLR § 5001, provides that “interest may be required by law.” Ultimately, the court concluded that “[g]iven the tension between Rule 44(d) and Section 5001, it is appropriate to refrain from vacating an arbitral award and to defer to the arbitrators’ judgment. This case was partially reversed on unrelated grounds in E.E. Cruz v. Coastal Caisson Corp., 346 Fed. Appx. 717 (2d Cir. 2009).</td>
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<td><em>P.M.I. Trading Ltd. v. Farstad Oil, Inc.</em>, 2001 U.S. Dist. LEXIS 227 (S.D.N.Y. 2001)</td>
<td>In this New York Convention case, the court, citing <em>Waterside Ocean Nav.</em>, held that, absent persuasive evidence to the contrary, post-award, prejudgment interest is available for judgments rendered under the New York Convention and is presumed to be appropriate. The court held that “[t]he mere fact that arbitrators chose not to award post-award, prejudgment interest does not control this analysis.” It granted post-award, prejudgment interest, as well as post-judgment interest, at the federal post-judgment rate specified by 28 U.S.C. § 1961(a).</td>
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<td>11</td>
<td><em>Shamah v. Schweiger</em>, 21 F.Supp.2d 208 (E.D.N.Y. 1998)</td>
<td>In this proceeding to confirm a domestic arbitral award, the award-creditor moved to modify the amount of the award to include pre-award interest at the New York statutory prejudgment interest rate of 9%. It asserted that the tribunal’s grant of 6% interest was a “material miscalculation” that necessitated modification. The court denied the motion, noting that courts “have rejected motions to vacate or modify arbitration awards which have failed to provide prejudgment interest.” The court also cited <em>Moran v. Arcano</em> for the proposition that arbitrators may grant pre-award interest, but when their award is silent with regard to such interest, courts may not grant it in the arbitrators’ stead. The court considered that, in awarding 6% interest, the tribunal could have been using the federal post-judgment interest rate. Accordingly, there was no evidence that the pre-award interest component of the arbitral award was miscalculated. The court denied the award-creditor’s request for modification.</td>
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| 12  | *Nicoletti v. E.F. Hutton & Co.*, 761 F.Supp. 312 (S.D.N.Y. 1991)             | The award-creditor moved to modify a domestic arbitral award on the ground that the tribunal had manifestly disregarded the law in failing to grant him pre-award interest under CPLR § 5001. The court denied the motion, noting that the award-creditor had cited to no case in which an arbitration
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<td>award was vacated or modified for failure to award prejudgment interest. Although the award-creditor’s claim sounded in contract, the arbitrators may have determined that his entitlement was equitable rather than contractual, and that interest was therefore discretionary under CPLR § 5001(a).</td>
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<td><em>Jamaica Commodity Trading Co. v. Connell Rice &amp; Sugar Co.</em>, No. 87 CIV. 6369 (JMC), 1991 WL 123962 (S.D.N.Y. July 3, 1991)</td>
<td>In this New York Convention enforcement proceeding, the arbitral tribunal had granted post-award, prejudgment interest “in the amount of 10% per year from the date of the award until the award is fully paid or reduced to judgment.” In addition to confirming the principal amount of the award, the court expressly noted that it was confirming the arbitrators’ award of prejudgment interest pursuant to <em>Waterside Ocean Nav.</em></td>
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<td>14</td>
<td><em>Moran v. Arcano</em>, 1990 U.S. Dist. LEXIS 9349 (S.D.N.Y. 1990)</td>
<td>In this proceeding to confirm a domestic arbitral award, the award-creditor claimed pre-award and post-award, prejudgment interest. The court held that whether interest is taxed on a claim prior to the entry of an arbitration award (i.e., pre-award interest) is within the discretion of the arbitrators (although neither of the two cases that it cited in support of this proposition so held). The court held that if the award is silent as to pre-award interest, a court is not entitled to grant it. By contrast, it held that “the award of post-award prejudgment interest is a matter left with the district court.”</td>
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<td>15</td>
<td><em>Brandeis Intsel, Ltd. v. Calabrian Chemicals Corp.</em>, 656 F.Supp. 160 (S.D.N.Y. 1987)</td>
<td>In this proceeding to confirm an international arbitral award under the New York Convention, the award-debtor cross-moved for vacatur, <em>inter alia</em> on the ground that the tribunal’s award of 11.5% pre-award interest was penal and therefore contrary to U.S public policy. The court denied the cross-motion, holding that the award-debtor had not shown that the arbitrators’ chosen rate of 11.25% per annum was penal as a matter of English law, which governed the parties’ contract. Moreover, the award-debtor had not pointed to any other expression of accepted public policy which would weigh against confirming the arbitrators’ award of interest. 28 U.S.C. § 1961(a), which refers to post-judgment interest, was inapposite.</td>
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<td>16</td>
<td><em>UCO Terminals, Inc. v. Apex Oil Co.</em>, 583 F. Supp. 1213 (S.D.N.Y. 1984)</td>
<td>In this proceeding to confirm a domestic arbitral award, the award-debtor cross-moved to vacate the award, in part on the ground that the tribunal’s calculation of post-award interest was incorrect and unauthorized. The tribunal had granted post-award interest at a rate of 12%, to run beginning 30 days after the award was rendered. The court rejected the award-debtor’s argument that this grant of interest was unauthorized, noting that “[p]ost-award interest is an entirely rational arrangement established by the arbitrators to compensate [award creditor] for its loss... Absent some express limitation on such an award, the Court can discern</td>
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<td>no disregard of applicable law or of the [underlying contract] here.”</td>
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<td>The court further rejected the award-debtor’s argument that the annual rate of 12% established in the arbitral award should be set aside, as there was no indication that the tribunal disregarded the law in granting such a rate of interest.</td>
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<td>17</td>
<td><em>A/S Siljestad v. Hideca Trading, Inc.</em>, 541 F. Supp. 58 (S.D.N.Y. 1981)</td>
<td>In this confirmation proceeding, the award-debtor moved to vacate the arbitral tribunal’s grant of pre-award interest at 14%, as said interest was omitted from the arbitral award itself and was only later added as an “Appendix B.” The award-debtor argued that this amounted to an impermissible reconsideration of the tribunal’s ruling.</td>
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<td>The court rejected the award-debtor’s claim, holding that the tribunal had not considered the issue of interest in its initial award, and therefore retained discretion to subsequently add pre-award interest in the form of Appendix B.</td>
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<td>The grant of interest was thus confirmed. The court, applying federal maritime law, granted post-award, prejudgment interest, also at 14%.</td>
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<td><em>United States use of Groisser &amp; Schlager Iron Works, Inc. v. Walsh</em>, 240 F. Supp. 1019 (N.D.N.Y. 1965)</td>
<td>In this case, the award-debtor moved to vacate a prior judgment confirming an arbitral award. The prior judgment had granted pre-award interest to the award-creditor notwithstanding that (a) the tribunal had not granted pre-award interest, and (b) the issue of interest had not been placed before the arbitral tribunal.</td>
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<td>The court held that, under CPLR §§ 5001, 5002 and 5003, the award-creditor was entitled to interest as a matter of right. The court noted that while the issue of interest was not submitted to the tribunal in the demand for arbitration, the parties specifically agreed in their arbitration agreement to arbitrate their dispute “as to balance due, together with appropriate interest.” Further, the award-creditor had demanded interest in the complaint it submitted to the district court.</td>
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<td>Thus, even though the arbitral tribunal had not granted pre-award interest, the court rejected the award-debtor’s argument that the court’s grant of pre-award interest was improper and merited vacatur or modification of the prior judgment.</td>
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<td>N.B. This case appears at odds with the weight of subsequent case law, which unambiguously holds that courts may not grant pre-award interest if the arbitrators have not done so.</td>
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New York state case law mirrors federal case law with regard to the review of arbitrators’ awards of interest.
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<td><em>Dermigny v. Harper</em>, 6 N.Y.S.3d 561 (2d Dep’t 2015)</td>
<td>In this appeal, the award-creditor sought to reinstate a vacated lower court judgment that had confirmed an arbitral award and granted pre-award interest. The lower court had vacated its own judgment on the ground that the award-creditor had misrepresented to the clerk of the court that he was entitled to pre-award interest. The Appellate Division noted that, because the arbitration award did not include a provision granting pre-award interest to the award-creditor, the court was without power to grant such pre-award interest. Post-award, prejudgment interest and post-judgment interest were granted pursuant to CPLR 5002 and 5003, respectively.</td>
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<td>20</td>
<td><em>Esrey v. Ernst &amp; Young, LLP</em>, 133 A.D.3d 539 (1st Dep’t 2015)</td>
<td>In this case, the award-creditors appealed from a lower court ruling denying a motion to vacate an arbitral award on the ground that the tribunal had manifestly disregarded the law by granting prejudgment interest at a rate lower than the CPLR rate. The First Department affirmed the trial court’s ruling, noting that (a) the parties’ agreement limited the prevailing party’s damages to the actual damages suffered and (b) the tribunal had found that the award-creditors were “fully compensated” by reduced prejudgment interest.</td>
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<td>21</td>
<td><em>Peters v. Collazo Florentino &amp; Keil LLP</em>, 117 A.D.3d 432 (1st Dep’t 2014)</td>
<td>In this case involving a domestic arbitral award, the award-creditor appealed from a decision confirming an arbitral award which granted prejudgment interest at a rate of 2% per annum. The First Department, reviewing the award under CPLR Article 75, denied the appeal and held that (a) the award-creditor failed to timely move to modify the award to raise the prejudgment interest rate to 9%, and (b) in any event, the arbitrator properly set the prejudgment interest rate at 2%. It is not entirely clear why the court felt that the 2% rate was proper. The court cited to CPLR § 5001(a), suggesting that it may have viewed the dispute as one of an equitable nature rather than for breach of contract. CPLR § 5001(a) provides that “in an action of an equitable nature, interest and the rate and date from which it shall be computed shall be <em>in the court’s discretion</em>.”</td>
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<td>22</td>
<td><em>Kingdon Capital Mgt., LLC v. Kaufman</em>, 110 A.D.3d 648 (1st Dep’t 2013)</td>
<td>In this case involving a domestic arbitral award, the award-debtor appealed from the lower court’s judgment granting the award-creditor the sum and prejudgment interest rate set by the award. The First Department unanimously affirmed the lower court judgment, noting that there was no basis for modifying the rate of prejudgment interest awarded.</td>
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<td>23</td>
<td><em>Levin &amp; Glasser, P.C. v. Kenmore Property, LLC</em>,</td>
<td>In this case involving a domestic arbitral award, the award-debtor appealed from the lower court’s</td>
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<td>Grobman v. Chernoff, 881 N.Y.S.2d 458 (2d Dep’t 2009)</td>
<td>The award-creditor appealed from a lower court order that disallowed pre-award interest. The circumstances of this case were unusual, in that the arbitration was focused solely on the issue of damages after the award-debtor’s liability had been determined in a prior jury trial. The Appellate Division observed that in a personal injury action in which the trial is bifurcated, interest on damages runs from the date liability is determined. Therefore, the court held that the award-creditor was entitled to “pre-award” interest, i.e. interest running from the date of the jury verdict that preceded the arbitration. Thus, the Appellate Division granted the award-creditor interest on her personal injury award from the date the award-debtor’s liability was determined, notwithstanding the tribunal’s silence with regard to pre-award interest. This decision was affirmed by the Court of Appeals in Grobman v Chernoff, 15 N.Y.3d 525 (2010).</td>
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<td>West Side Lofts, Ltd. v. Sentry Contr., Inc., 300 A.D.2d 130 (1st Dep’t 2002)</td>
<td>In this case involving a domestic arbitral award, the award-debtor appealed from a lower court ruling confirming an arbitral award, including pre-award interest. The First Department affirmed the lower court’s judgment. It held that, [g]iven a broad arbitration clause and the absence of a contractual provision specifically prohibiting preaward interest, the award of preaward interest cannot be successfully challenged as beyond the arbitrator’s power simply because the parties’ contract contains no provision therefor and petitioner made no such demand in the arbitration.”</td>
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<td>26</td>
<td>Rothermel v. Fidelity &amp; Guarantee Ins. Underwriters Inc., 721 N.Y.S.2d 565 (3d Dep’t 2001)</td>
<td>In this case involving a domestic arbitral award, the award-creditor appealed from a lower court ruling denying his request for pre-award interest. The arbitral tribunal had also refused to grant pre-award interest. The Appellate Division affirmed the lower court’s ruling, holding that the question as to whether pre-award interest is to be awarded is for the arbitrator to determine and, if the arbitrator does not award any pre-award interest, the court is powerless to do so.</td>
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<td>The court added that even if the arbitrator had committed an error of fact or law in denying the award-creditor pre-award interest, the lower court would have lacked the authority to correct such an error.</td>
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</table>
| 27  | *Excelsior 57th Corp. v. Kern*, 283 A.D.2d 209 (1st Dep’t 2001)               | The award-creditor appealed from a lower court judgment vacating so much of an arbitration award as granted pre-award interest.  
The Appellate Division affirmed the lower court, holding that the arbitrators exceeded their authority in awarding pre-award interest on the back rent they found due, because (a) the parties’ narrow arbitration clause only covered specifically-mentioned issues of fact and (b) the parties did not agree to submit the issue of interest to the arbitrators.  The court also declined to use “judicial discretion” to award interest under CPLR 5001, criticizing the award-debtor’s conduct in the underlying arbitration. |
| 28  | *State Farm Mut. Auto. Ins. Co. v. Cordes*, 662 N.Y.S.2d 140 (2d Dep’t 1997)  | In this appeal, the Second Department reversed a lower court order that granted pre-award interest, in spite of the arbitral tribunal’s failure to do so.  
The Second Department noted simply that “[t]he court lacked the power to award pre-arbitration award interest.”                                                                                                                                                                                   |
| 29  | *Aetna Casualty and Surety Co. v. Rosen*, 650 N.Y.S.2d 29 (2d Dep’t 1996)      | In this appeal from a lower court judgment confirming an arbitral award, the Appellate Division modified the lower court’s ruling so as to omit the court’s award of pre-award interest.  
The Appellate Division explained that the lower court was powerless to grant pre-award interest (as presumably the tribunal had not provided for such interest).  Rather, upon confirmation of an arbitrator’s award, interest should be calculated from the date of the award. |
| 30  | *Sedlis v. Gertler*, 554 N.Y.S.2d 615 (1st Dep’t 1990)                         | In this appeal from a lower court judgment confirming a domestic arbitral award, the tribunal had granted pre-award interest and post-award interest at a rate of 12%.  The award-creditor requested that the court vacate the award or modify the interest the interest portion of the award.  
The parties’ contract provided that late payments would bear interest at the rate specified or at the “legal rate” at the award-creditor’s place of business, which was New York.  
The First Department held that, as no interest rate was specified in the parties’ contract, prejudgment interest should be calculated at the rate of 6% per annum set by General Obligations Law § 5-501(1).  
In modifying the award, the First Department relied on CPLR § 7511(c)(1), which provides that the court shall modify an arbitral award if “there was a miscalculation of figures . . . in the award.”  This appears to have been in error, given that CPLR § 7511(c)(1) only authorizes modification of computational errors and not reversal of substantive rulings.  The arbitrators’ award of interest involved a decision on a substantive |
<table>
<thead>
<tr>
<th>No.</th>
<th>Case Citation</th>
<th>Approach to Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>31</td>
<td><em>Gruberg v. Cortrell Group, Inc.</em>, 143 A.D.2d 39 (1st Dep’t 1988)</td>
<td>In this case involving a domestic arbitral award, the award-creditor appealed from a lower court judgment that had denied pre-award interest. The Appellate Division upheld the lower court’s decision to deny pre-award interest, but modified the date from which post-award interest was to run to correct a computational error by the arbitrator. The Appellate Division noted that in a contract dispute brought before an arbitrator, the question of whether interest from the date of breach of contract should be allowed is a mixed question of law and fact for the arbitrator to determine. Further, in a motion under CPLR § 7510 to confirm an arbitral award, the arbitrator’s award is deemed conclusive as to all matters of law and fact, unless some ground for modification or vacatur exists under CPLR § 7511. In this case, since the tribunal’s award was silent as to pre-award interest, the lower court did not have the authority to grant such interest.</td>
</tr>
<tr>
<td>32</td>
<td><em>Rosenblum v. Aetna Casualty &amp; Surety Co.</em>, 439 N.Y.S.2d 482 (3d Dep’t 1981)</td>
<td>The award-creditor appealed from a lower court judgment confirming an arbitral award that omitted pre-award interest. The award-creditor had moved under CPLR § 7511 to modify the award to include pre-award interest, but this motion was denied. The Appellate Division considered it “well settled” that arbitrators are empowered to fashion awards to achieve just results and “may shape remedies with a flexibility at least as unrestrained as that employed by a chancellor in equity.” Accordingly, the award should not be disturbed.</td>
</tr>
<tr>
<td>33</td>
<td><em>Penco Fabrics, Inc. v. Bogopulsky, Inc.</em>, 146 N.Y.S.2d 514 (1st Dep’t 1955)</td>
<td>In this proceeding involving a domestic arbitral award, the Appellate Division held that the question of whether interest is to be allowed from the date of breach was for the arbitrators to determine. The court was powerless to award interest from the date of breach. The mere fact that the award was silent on interest did not mean that the arbitrators did not consider this question. Additionally, the court noted that provisions of law applicable to judicial actions and proceedings do not necessarily apply to arbitrations. Parties who submit their disputes to arbitration forego these provisions and leave all questions of law and fact to the arbitrators. The right to interest involves questions of law and fact that were within the arbitrators’ purview.</td>
</tr>
</tbody>
</table>
| 34  | *Taborsky v. Bayes*, No. 09-9562, 2016 N.Y. Misc. LEXIS 592 (Sup. Ct. Suffolk Co. Feb. 23, 2016) | In this proceeding to confirm an arbitral award pursuant to CPLR Article 75, the award-creditor moved to modify the award to add pre-award interest, pursuant to CPLR § 5001. Citing *Dermigny* and *Rothermel*, the court noted that the arbitration award “did not include a provision
<table>
<thead>
<tr>
<th>No.</th>
<th>Case Citation</th>
<th>Approach to Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>35</td>
<td><em>Chamois v. Countrywide Home Loans, Inc.</em>, 863 N.Y.S.2d 897 (Sup. Ct., Orange Co., 2008)</td>
<td>In this proceeding to confirm a domestic arbitral award in a labor dispute, the award-creditors claimed that they were entitled to pre-award interest on their back pay award as a matter of law, despite the fact that the tribunal had not granted such interest. The court, applying the review standards contained within CPLR Article 75 and the Federal Arbitration Act, concluded that “judicial review of arbitration awards is extremely limited.” In particular, the court noted that arbitrators may provide for pre-award interest as part of their award, and that courts have rejected motions to vacate or modify arbitration awards which have failed to provide pre-award interest. It also noted that where an award is silent on pre-award interest, a court may not grant it. Thus, because pre-award interest was not mentioned in the arbitral award, the award-creditors’ request was denied.</td>
</tr>
<tr>
<td>36</td>
<td><em>DeMartini v. Bertram Garden Apartments</em>, 138 N.Y.S.2d 659 (Sup. Ct. Queens Co. 1955)</td>
<td>In this case involving a domestic arbitration, the arbitral tribunal had rendered an award, a judgment had been entered thereon, and the award-debtor had made payment in full. Nevertheless, the award-creditor contended that he was still entitled to continue a proceeding to enforce a mechanic’s lien for pre-award interest on the arbitral award. The arbitrator’s award had not provided for pre-award interest. The court noted that “interest was an incident of the award and arose out of the contract between the parties” because all matters arising out of that contract were within the scope of the parties’ arbitration agreement. It followed that the arbitral award and the judgment entered thereon stood as a bar to enforcement of the mechanic’s lien. The court thus granted summary judgment dismissing the award-creditor’s attempt to enforce the mechanic’s lien.</td>
</tr>
</tbody>
</table>
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INVALID ROUND TRIPS IN SETTING
PRE-JUDGMENT INTEREST IN
INTERNATIONAL ARBITRATION

Manuel A. Abdala, Pablo D. López Zadicoff, Pablo T. Spiller*

In spite of its crucial role in damage compensation, there is not a well-developed set of generally accepted principles of pre-judgment interest ("PJI") by arbitration tribunals. A typical mistake in international arbitration awards is the granting of PJI that is significantly lower than the rate used to discount cash flows. This often results in what we call "invalid round-trips" ("IRTs") in damage assessment. We also show that, from an economic perspective, full compensation requires in most cases that PJI be linked to the cost of capital of the affected business. Such rate would, under most circumstances, promote efficiency in the conflict resolution system.

I. INTRODUCTION

Pre-judgment interest (PJI), a key determinant of value in damage awards, is often overlooked by both tribunals and damage experts alike. Despite all the warnings in the literature, PJI still ranks last in tribunals’ pecking order of decisions,¹ while the perception that it is purely a legal issue, and its seeming relative simplicity, leads damage experts to not pay too much attention to this issue either. This has led to a multiplicity of PJI

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criteria, with choices often contradicting the underlying economics of the case, resulting not only in under-compensation, but also rewarding opportunistic behavior and providing incentives to delay both decision and payments of awards.

The longer the time between the breach and the final award, the more crucial the correct assessment of PJI becomes. The complexities and uniqueness of international arbitration cases often call for extended proceedings. For example, as of September 2010, of the 124 treaty cases in progress under ICSID jurisdiction, roughly half were started before 2008, and 30 before 2005. To the length of time cases take to reach final resolution we must add the fact that normally cases arise from events that occurred well before the date of filing – if awards are calculated following the date of the breach approach – PJI may accrue for a period of several years, becoming an important component of the overall compensation amount.

A few examples from ICSID awards issued during the last decade show the different approaches to PJI. In *Santa Elena v. Costa Rica*, the tribunal’s award included PJI for almost 22 years at a compound rate of approximately 6.4%, similar to the 6.0% compound rate awarded in a contemporaneous decision by the *Metalclad v. Mexico* tribunal, arising from a 7-year case. In *Archer Daniels Midland and Tate & Lyle v. Mexico*, the Tribunal set the PJI rate as the US 1-month T-bills (simple rate), which was, on average, 4.0% for the relevant 2005-2007 period. In *Desert Line*

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3 This assumes awards that are based on damage calculation as of the date of the breach. In some cases the valuation date could be set as of the date of the award, in which case the issue of PJI becomes moot. The present paper, however, does not focus on this latter situation.


5 See Compañía del Desarrollo de Santa Elena S.A. v. Republic of Costa Rica, ICSID Case No. ARB/96/1, Award (Feb. 17, 2000).

6 See Metalclad Corp. v. United Mexican States, ICSID Case No. ARB(AF)/97/1, Award (Aug. 30, 2000).

7 See Archer Daniels Midland Co. & Tate & Lyle Ingredients Am., Inc. v. United Mexican States, ICSID Case No. ARB(AF)/04/5, Redacted Award (Nov. 21,
Projects v. Yemen the PJI rate was set at an *ad hoc* rate of 5.0%, and was only applicable to part of the damages. In several recent international investment arbitrations, including *Sempra Energy v. Argentina* and *PSEG Global Inc. and Konya v. Turkey*, tribunals have granted pre-judgment interest at floating rates, based on the 6-month LIBOR commercial rate plus a 2 percentage point spread. In another recent case, *Siag v. Egypt*, the Tribunal granted PJI at the 6-month LIBOR (with no spread) for a period of 13 years.

As evidenced above, each of these decisions differs substantially in its underlying rationale for choosing PJIs. While some based their calculations upon *ad hoc* rates, others link PJI to market variables of dissimilar nature. Whatever the method, though, a key concern is the practice of awarding damages computed as discounting cash flows at risk-adjusted rates to the date of valuation, and then re-expressing those back to the date of award at substantially lower (risk-free or similar) rates. We call this practice an “invalid round-trip” (IRT). In *CMS v. Argentina*, for example, the Tribunal considered a discount rate ranging from 14.5% to 18.0% to calculate damages as of year 2000, but granted PJI up to 2005, the time of the award, at simple interest “at the annualized average rate of 2.51% of the United States Treasury Bills.”

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8 See Desert Line Projects LLC v. The Republic of Yemen, ICSID Case No. ARB/05/17, Award (Feb. 6, 2008) (imposing a 5% PJI rate on the enforcement of the Yemeni Arbitral Award but not on the calculation of moral damages).

9 See PSEG Global Inc. and Konya Ilgin Elektrik Üretim ve Ticaret Limited Sirketi v. Republic of Turkey, ICSID Case No. ARB/02/5, Award (Jan. 19, 2007). See also *Sempra Energy Int’l v. Argentine Republic*, ICSID Case No. ARB/02/16, Award (Sep. 28, 2007).

10 See Waguih Elie George Slag and Clorinda Vecchi v. The Arab Republic of Egypt, ICSID Case No. ARB/05/15, Award and Dissenting Opinion (June 1, 2009).

11 See *CMS Gas Transmission Co. v. Argentine Republic*, ICSID Case No. ARB/01/08, Award, ¶¶ 450-455 (May 12, 2005).
In this article we discuss the implications of IRTs, and focus on the selection of the proper PJI rate when analyzed from financial and economic perspectives.

II. INVALID ROUND-TRIPS: DEFINITION

An IRT occurs whenever the PJI is set at a rate that differs substantially from the rate at which expected future losses are discounted to the valuation date. Except in extremely simplified cases where all damages are generated simultaneously with the event that causes them, the damage calculation process normally requires aggregating multiple and sequential reductions in cash flows into a single value as of the date of valuation (the date of breach). Normally, discount rates account for the time value of money and the systematic (non-diversifiable) risk of the business under analysis in computing this aggregation.\(^{12}\)

On the other hand, compensation to claimants is necessarily paid sometime following the date of the award. To express the amount of compensation from the date of valuation to the date of award, tribunals apply a second rate as a PJI, which normally differs from the discount rate at which the expected lost profits are discounted. This is the essence of the “round-trip” of cash flows through the tunnel of time. The value of future cash flows are discounted in time to express value as of the date of breach (Trip One) and then such value has to be converted into value at a later time, often the date of the award (Trip Two).

A. IRTs Involving Historical Losses

This Article first considers a simple example of what is normally called “historical damages,” that is, damages related to cash-flows foregone before the date of the award. Assume that a breach imposes two consecutive and equal yearly losses to claimant of $100. Call the time of the breach Year 0. The first loss is simultaneous with the breach, and the second occurs a year

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\(^{12}\) The use of discount rates could be explicit — as under a Discounted Cash Flow (“DCF”) methodology — or implicit — as when valuing using market information to assess value. It is a well known principle in financial valuation that the stock price of an asset is related to the underlying risk-adjusted cash flows that are expected to be generated.
later (Year 1). The nominal amount of damages, without any
discounting or actualization, is then worth $200. A Tribunal
awarding damages, say two years after the breach (at Year 2), is
presented with four scenarios:

a) To first value the losses, as of the date of the breach, by
discounting each loss to the date of the breach at a risk-
adjusted rate, say 15%, and then to express such value as
of the date of the award at a risk-free PJL, say 3%. Compensations will be equal to $198.$13

b) Same as (a) but using the same risk-adjusted rate (the 15% 
business cost of capital) as PJL. Compensation will result in
$247.$14

c) To avoid the discount-compound loop and directly bring
forward nominal losses as of the date of the award, at a
risk-adjusted rate such as the business’ cost of capital – say
15%. The compensation amount here will be $247, the
same as alternative (b)$15

d) Same as (c), but bringing forward each $100 lost to the
date of the award at a risk-free rate, say 3%. Compensation will equal $209.$16

In all cases the value of the cash flows at the date of breach is
exactly the same ($187).$17 The examples above and outcomes are
numerically illustrated in Table I, which presents the amounts
awarded under the different scenarios, and how each yearly
nominal loss is considered in each calculation. For instance, under
scenario (a) damages are calculated as $198, which are in turn
composed of $106 related to the Year 0 loss, and $92 related to
the Year 1 loss.

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13 The exact compensation is $198.34 = (100+100/1.15)*1.03^2 = 186.96*1.03^2.
14 The exact compensation is $247.25 = (100+100/1.15)*1.15^2 = 186.96*1.15^2.
15 That this is identical to (b) can be seen because (100+100/1.15)*1.15^2 =
100*1.15^2+100*1.15, which is equivalent to just bringing forward the yearly
losses to the date of the award.
16 The exact compensation is $209.09 = 100*1.03^2+100*1.03 = 106.09 + 103.
17 The exact value is $186.96= (100+100/1.15).
Table I: Example of IRT with Historical Losses  
(All $ Values in currency of the Date of Award)

<table>
<thead>
<tr>
<th>Scenario</th>
<th>Discount Rate (Trip 1)</th>
<th>PJI Rate (Trip 2)</th>
<th>Date of the Breach (Year 0)</th>
<th>Year 1 Loss</th>
<th>Total Award</th>
</tr>
</thead>
<tbody>
<tr>
<td>N/A</td>
<td>N/A</td>
<td>$100</td>
<td>$100</td>
<td>$200</td>
<td></td>
</tr>
<tr>
<td>Scenario (a)</td>
<td>15%</td>
<td>3%</td>
<td>$106</td>
<td>$92</td>
<td>$198</td>
</tr>
<tr>
<td>Scenario (b)</td>
<td>15%</td>
<td>15%</td>
<td>$132</td>
<td>$115</td>
<td>$247</td>
</tr>
<tr>
<td>Scenario (c)</td>
<td>N/A</td>
<td>15%</td>
<td>$132</td>
<td>$115</td>
<td>$247</td>
</tr>
<tr>
<td>Scenario (d)</td>
<td>N/A</td>
<td>3%</td>
<td>$106</td>
<td>$103</td>
<td>$209</td>
</tr>
</tbody>
</table>

An IRT plainly occurs under scenario (a), resulting in dramatic under-compensation of the claimant as the damages computed under this method are less than $200 or the nominal value of the historical damages. Since the award comes after the damage was inflicted, the award should at least compensate claimant for the nominal value of the loss, even if disregarding all considerations for the time value of money. Scenario (a), however, fails to accomplish even that.

Scenarios (b) and (c) provide claimant with equivalent compensation. Scenario (b) involves two trips (one to discount cash flows to the date of valuation and another to bring them forward to the date of the award), it does not involve an IRT as it uses the same rate to both discount and bring forward damages. Scenario (c) avoids discounting damages back to the date of breach and directly compounds them to the date of award at the risk-adjusted rate.

Scenario (d) also does not involve an IRT, as it does not first discount historical damages to the date of the breach. Although compensation of the claimant under this scenario exceeds the nominal $200 loss, it nevertheless fails, in most cases, to provide full compensation. As we discuss below, the PJI rate must under most circumstances be commensurate to the risk of doing business in the affected activity, and thus, to its cost of capital (in this case 15%).

B. IRTs Involving Future Losses

IRTs may also involve future losses, not just historical damages. Expanding upon the prior illustration, assume now that the losses attributable to the breach are expected to go beyond
the two historical years, and actually expand into the future with identical nominal yearly losses of $100 for a total of six consecutive years. Assume further, like in our prior example, that claimant’s business operates in an environment where the cost of capital is 15%.

Table II illustrates, as in the previous table, the numerical example of the four scenarios (a) to (d). Accordingly, we calculate the value awarded for each yearly nominal loss of $100 under the four alternative scenarios. For instance, under scenario (a) total damages awarded amount to $462, composed of $106 related to the Loss of Year 0, $92 to the loss of Year 1, and so on. The arrows represent the direction of discounting and compounding of cash-flows: Scenarios (a) and (b) first discount back all cash-flows, historic and future, to the date of breach at the 15% discount rate, and then compound back the result to the date of award at the corresponding PJI for each scenario. Scenarios (c) and (d) directly compound or discount future cash-flows to the date of award at the relevant rates, without first discounting them to the date of the breach.18

Table II: Example of IRT with Future Losses
(All $ Values in currency of the Date of Award)

<table>
<thead>
<tr>
<th>Nominal Losses</th>
<th>Date of Breach (Year 0 Loss)</th>
<th>Year 1 Loss</th>
<th>Date of Award (Year 2 Loss)</th>
<th>Year 3 Loss</th>
<th>Year 4 Loss</th>
<th>Year 5 Loss</th>
<th>Total Award</th>
</tr>
</thead>
<tbody>
<tr>
<td>$100</td>
<td>$100</td>
<td>$100</td>
<td>$100</td>
<td>$100</td>
<td>$100</td>
<td>$100</td>
<td>$600</td>
</tr>
<tr>
<td>Scenario (a)</td>
<td>$106</td>
<td>$92</td>
<td>$80</td>
<td>$70</td>
<td>$61</td>
<td>$53</td>
<td>$462</td>
</tr>
<tr>
<td>Scenario (b)</td>
<td>$132</td>
<td>$115</td>
<td>$100</td>
<td>$87</td>
<td>$76</td>
<td>$66</td>
<td>$576</td>
</tr>
<tr>
<td>Scenario (c)</td>
<td>$132</td>
<td>$115</td>
<td>$100</td>
<td>$87</td>
<td>$76</td>
<td>$66</td>
<td>$576</td>
</tr>
<tr>
<td>Scenario (d)</td>
<td>$106</td>
<td>$103</td>
<td>$100</td>
<td>$87</td>
<td>$76</td>
<td>$66</td>
<td>$537</td>
</tr>
</tbody>
</table>

18 Observe that all scenarios are valuing damages as of the date of breach, as expectations of cash flow losses (the $100 yearly losses) are based on date of breach expectations. We are not dealing here with the issue raised in Chorzów Factory of whether valuation should be performed as of the date of breach or the award. See infra note 23. For a discussion on this topic, see Manuel A. Abdala & Pablo T. Spiller, Chorzów’s Standard Rejuvenated: Assessing Damages in Investment Treaty Arbitrations, 25 J. INT’L ARB. 103 (2008).
In the example above, note that, given that a major part of the damages arise from cash flows that were to be collected after the date of award (i.e., losses expected in Years 3 to 5), all scenarios show that the $600 worth of nominal damages should be compensated with an award of a lesser amount. The rationale is that these are lost profits not yet incurred but expected to be lost in the future (when standing as of the date of the award) and thus are discounted at the risk-adjusted discount rate of the business (15% in this example).

In scenarios (a) and (b), all future cash flows are discounted to the date of breach by using the risk-adjusted 15% rate (Trip 1) and then expressed as of the date of award using a PJI of 3% and 15%, respectively (Trip 2). As in the previous example, scenario (a) fails to provide compensation of at least the $200 nominal amount lost in the first two “historical” periods (Losses of Years 0 and 1). More evident is the fact that, when applied to the cash-flow contemporary to the date of award (Year 2), scenario (a) implies that a nominal cash-flow of $100 that claimant expected to collect at the date of the award is only compensated at $80 due to the imposition of an artificial IRT.

Also, when applied to future cash flows, the IRT of scenario (a) results in discounting cash flows in excess of the measure of risk applicable to them. For example, the Year 3 cash-flow which was to occur one year after the date of award is valued at $70, which would be roughly the result of applying a 40% discount rate for a year. As a consequence, in this example, the IRT implicit in scenario (a) is equivalent to the application of a discount rate to the cash flows of the first year past the date of the award that more than doubles that of the cost of capital of the business (15%).

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19 The exact compensation is $69.76 = (100/1.15^3)*1.03^2.
20 100/1.40=71.42.
21 In the same manner, it can be seen that the implicit discount rate arising from the IRT of this scenario is 27% for the loss in Year 4 and 23% for the loss in Year 5. These discount rates are substantially above the assumed cost of capital of the affected business (15%).
On the other hand, scenario (b) applies the discount rate used for discounting cash flows in the calculation of PJI (hence avoiding the IRT), providing proper compensation of the historical damages arising from "historical" cash-flows. As for future profits, it properly awards the nominal amount of damages at Year 2 (those contemporary to the date of award) and discounts future damages to the date of the award exclusively by the appropriate 15% risk-adjusted rate.

The difference between the $576 awarded to claimant under scenario (b) and the $462 awarded under scenario (a) is the consequence of the IRT, by which each affected cash flow, whether historical or future, is artificially diminished by the differential between the business discount rate and the PJI, with the impact increasing in the distance in time between the date of the breach and the date of the award.

While scenario (c) once again avoids the unnecessary discount-compound loop, compensation awarded is analogous to scenario (b). Scenario (d) in turn avoids incurring an IRT, resulting in the same compensation as scenarios (b) and (c) for damages related to all future periods from the date of award on (i.e., since Year 2), while very likely failing to provide fair compensation for previous losses, as will be further discussed.

The impact of the IRT is increased both by the difference between the discount rate and the PJI rate, as well as by the time that elapses between the date of breach and the date of the award; thus, comparing scenarios (a) and (b), the IRT effect of $114 (calculated as $576 – $462) falls to $49 if the PJI is raised to 10% in scenario (a) and increases to $140 if no PJI at all is granted. Similarly, should the date of award be Year 1 (instead of Year 2), the IRT effect on damages of scenario (a) would be of $52 (compared to $114 of our original example), while a date of award in Year 4 would increase the IRT effect to $271.

It becomes evident from the above discussion that the only way to avoid an IRT and preserve the value of the cash flows
subject to the damage analysis is to grant PJI at the “same rate(s)” used to discount future cash flows.22

III. INVALID ROUND TRIPS AND THE VIOLATION OF THE FULL COMPENSATION PRINCIPLE

It is an accepted principle of international law that awards should grant full compensation, that is, that they should restore claimant to the position it would be had the contested actions not been taken.23 This Article shows next that, under most circumstances, the cost of capital of the affected business is not only the rate which avoids IRT (as shown above) but which also satisfies this principle.

From an economic perspective, full compensation requires that both the impact of the damaging actions and the nature of the judicial process be taken into account.24 Although tribunals attempt to provide full compensation by taking the impact of the damaging actions into account, their choice of PJI is seldom consistent with the delay between the date of the breach and the date of the award.

In most cases, a claimant who wins on the merits in an international arbitration has operated a business which has been deprived of some (or all) of its cash flows. The deprivation of these cash flows limited the ability of the company to pay dividends or repay its debt. This implies that shareholders and lenders will demand compensation for the delayed cash flows at

22 We refer to the “same rate” in a conceptual rather than in a strict way. Accordingly, for example, the use of different risk-free rates or risk-adjusted rates for each year is not considered different, but rather the mix of risk-free rates (to compound) and risk-adjusted rates (to discount). Moreover, for simplicity we are currently not making a distinction between cost of equity and cost of capital of the affected business. The general rule is that when considering damages to the firm the latter should be used, while the former is more appropriate when dealing with equity losses.

23 The principle of full compensation in international arbitration is closely linked to the Chorzów Factory’s dixit, aimed to “wipe out all the consequences of the illegal act and re-establish the situation which would, in all probability, have existed if that act had not been committed.” See Factory at Chorzów, (Ger. v. Pol.), 1928 P.C.I.J. (ser. A) No. 13, at 47 (Sept. 1928).

24 See Colon & Knoll, supra note 1, at page 2.
their respective costs of capital (cost of equity and cost of debt), as no investor would have willingly postponed the collection of these proceeds at a lower rate from the company. In other words, the deprivation of cash flows implied a financing cost equivalent to the cost of capital of the affected business. Thus, to make claimant whole, the financing costs associated with the delay ought to be taken into account as well. The damaged business’ cost of capital is the rate that, on average, makes the damaged party indifferent between cash flows across different dates.

Financial literature also supports the view that the cost of capital of the affected business is the appropriate PJI rate that satisfies full compensation.\(^\text{25}\) Recently, for example, several authors have presented conclusions similar to ours. Escher and Krueger put forward a theory for granting PJI at the plaintiff’s cost of capital.\(^\text{26}\) Gotanda and Sénéchal, however, advocate the use of a generic cost of capital irrespective of the claim, based on the average cost of capital of the market.\(^\text{27}\) Although Professors Gotanda and Sénéchal agree that the cost of capital of the affected asset as measured by the WACC (weighted average cost of capital) is a proper theoretical measure for PJI, they recommend the use of a risk-adjusted rate as PJI, measured as the sum of the risk-free interest rate and the market risk premium, instead of the specific cost of capital because, in their view, it might be difficult to compute cost of capital for non-traded companies or in certain countries, where data is scarce. Furthermore, they suggest that the complexity of the cost of capital calculation, a project-specific task, could trigger an unnecessary “battle of the experts.”\(^\text{28}\)

\(^{25}\) The cost of capital is also in general terms recognized by the financial literature as the threshold rate that determines the profitability of an investment option which follows our rationale on the discussion of full compensation. See, e.g., Richard A. Brealey & Stewart C. Myers, *Principles of Corporate Finance* (2006) (discussing in Part II, Chapter 7 the risk and cost of capital).

\(^{26}\) Susan Escher & Kurt Krueger, *The Cost of Carry and Prejudgment Interest*, 6 LITIGATION ECON. REV. 12 (2003) (following a similar rationale to ours, although technically more complex, when advocating for the use of the claimant’s cost of capital as the relevant PJI rate based on Keynes’ “cost of carry” principle and its implications over future contracts).

\(^{27}\) See Gotanda & Sénéchal, *supra* note 1.

\(^{28}\) Id.
Although quite close to the concept of cost of capital, this proposal does not include a measure of the additional risk components faced by the affected business, such as regulatory risk, country risk premium and size premium, among others.29

In our view, while the alleged conceptual and computational difficulties are there, these challenges are not insurmountable, and should not stop tribunals from using the appropriate cost of capital as PJI for at least three reasons. First, the computation of the elements of the WACC, although project specific, are based on optimal market standards. Elements such as the Beta, or the debt/equity ratio, must be based on the standards of the industry, rather than that of the company itself, resembling what willing buyers and willing sellers would do in assessing the cost of sourcing capital to optimize value.30 Second, valuation experts can cope with the difficulties of the computation of the cost of capital, by using standard methodologies from corporate finance.31 Third, the affected business’ cost of capital will most likely be used in the arbitration proceedings for the much debated discount rate, and thus should be already part of the experts’ opinions, available in the arbitration records. Thus, the potential “battle of experts” will naturally arise as to the level of cost of capital independently of the choice of PJI.32

A. Alternative Views on PJI and the Achievement of Full Compensation

Fisher and Romaine, among other authors, have recommended the use of a banking (risk-free) deposit rate as PJI.33 The authors assert that, since claimants ought to have been compensated at the time of the breach, they should have cashed out the value of their investment at that point in time, relieving

29 Id.
30 See BREALEY & MYERS, supra note 25, at 221, (“The precision of the portfolio beta is better than that of the betas of the individual companies.”).
31 Id.
32 Id.
them from the part (or the totality) of the project’s risks going forward.\(^{34}\) Although there may be special circumstances under which full compensation can be achieved by granting a risk-free rate as PJI, as discussed above, this is not the default case.\(^{35}\)

Other authors, such as Knoll and Colon have recommended a PJI rate linked to the respondent’s cost of debt (the so-called “coerced loan” theory) assuming that, at the date of the breach, an implicit transaction took place, by which claimant exchanged the value of its damaged stake for debt of the respondent.\(^{36}\) This approach has several shortcomings.

As noted by one scholar, fixing the PJI at the respondent’s market cost of debt is insufficient when information and the possibility to transfer claims are limited.\(^{37}\) Before the breach, claimant had a right to certain assets (and its corresponding expected return on such assets) that it could trade in the market. The arbitration procedure implies that claimant is forced to hold on to another asset, the potential forthcoming award of damages, of uncertain value for an uncertain period of time. Claimant’s demand for damages is unlike a bond (based on the coerced loan theory) which has a defined payment schedule and can be traded in the market, calling for a liquidity premium. It is unlikely that this liquidity premium would imply a cost of debt that would match the cost of capital of the affected business. In some cases the liquidity premium on respondent’s cost of debt could be high enough to imply a PJI rate well in excess of the cost of capital of the affected business.\(^{38}\) For example, Argentina has had multiple

\(^{34}\) Id. at page 146 (justifying their position by arguing that it is customary in U.S. courts not to recognize the costs of litigation, among which the delay in collection could be considered).

\(^{35}\) As we discuss below, in cases where the affected business exits voluntarily (i.e., for reasons unrelated to the breach), from the date of exit onwards, claimant’s financing cost (i.e., the rate that recognizes the delay in the collection of cash flows imposed by the damage) is unlinked from its cost of capital.

\(^{36}\) See Knoll, A primer on Prejudgment Interest, 75 Tex. L. Rev. 293; Colon & Knoll, supra note 1, at page 3-4.

\(^{37}\) See Patell et al., supra note 1.

\(^{38}\) Other reasons are the increasing marginal cost of funding (i.e., the fact that to raise a significant amount of additional debt the issuer must raise its interest
claims arising from alleged treaty breaches in early 2002, the time when Argentina’s debt entered into default and traded at discounts reaching 50-70% (implying exorbitant formal yields to maturity, but more realistically, showing low expectations of recovery). If tribunals were to determine the PJI under the coerced loan theory, this may result in dramatic over-compensation.39

In sum, the two main competing arguments to the use of cost of capital as PJI, namely, the use of risk-free rates and the coerced loan theory both have the potential to result in IRTs and result in either under-compensation or over-compensation of the claimant.

IV. INVALID ROUND TRIPS AND INEFFICIENCIES

The particular choice of PJI may also have efficiency implications. Since breaching parties normally benefit from the breach (such as when a government expropriates an asset, or illegally raises taxes), the capture of the associated cash flows reduces its need to source funds in the open market at risk-adjusted rates.

It follows then, that if the PJI rate is lower than respondent’s cost of raising funds (and ignoring any reputation considerations that may affect future endeavors), it becomes cheaper for a potential offender to raise funds by breaching investment contracts than by sourcing in the open market.40 Furthermore, a

rate, and the preferences of the claimant who may have chosen not to buy debt from the respondent at the prevailing market rates. Colon and Knoll also acknowledge a limitation to the use of the respondent’s cost of debt when a large share of claimant’s wealth is tied up in the claim. See Colon & Knoll, supra note 1, at pages 14-15.

39 We know of no Argentine treaty case in which a Tribunal awarded PJI based on the coerced loan theory. We are also unaware of any claimant requesting PJI based on this theory.

40 For example, suppose that a government has a cost of debt of 10% and knows that if it commits a damaging act it expects to be subject to a PJI rate of 5% on the market value of the damage. If today the government issues a 1-year bond for $100, it should expect to pay $110 at cancellation (at a 10% cost of debt). Conversely, the government can levy a one-time “expropriatory tax” of $100 to a company, which will be repaid by means of an arbitration award. Assuming that the arbitral procedure lasts 1 year, using a PJI rate of 5%, the award will have a value of $105, lower than the debt repayment.
PJI lower than respondent's cost of raising funds provides it with incentives to delay the arbitration process, so as to continue benefitting from the lower “financing” rate. Therefore, to guarantee the efficiency of the conflict resolution system, the PJI has to be no lower than the respondent’s cost of raising funds.

The affected business’ cost of capital (i.e., the rate that avoids IRTs) will typically be equal or above the respondent's cost of debt, therefore guaranteeing efficiency, although under some circumstances such may not be the case. The high cost of debt in Argentina’s treaty arbitrations mentioned above would be a good example of how considerations based only on the efficiency principle would call for unreasonable outcomes that could result in significant overcompensation, since respondent’s cost of debt would have been well above the cost of capital of the business subject to the alleged breach. Therefore, respondent's cost of debt in such case, albeit meeting the test of efficiency, is likely to lead to overcompensation, violating the full compensation principle. Whether the efficiency principle should be waived under these circumstances escapes the current economic analysis.

V. THE AFFECTED BUSINESS’ COST OF CAPITAL AS THE RELEVANT PJI BENCHMARK

Although the use of the affected business’ cost of capital as PJI is the only rate that can avoid the occurrence of IRT, while also achieving full compensation, there are various misconceptions about its use as the PJI benchmark.

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41 Debt is typically a more economical source of funding than equity. The cost of capital is a weighted average cost of sourcing capital between equity and debt. When the parties to the arbitration are not very dissimilar in terms of risk, the respondent’s cost of debt will tend to be lower than the affected business’ cost of capital.

42 In fact, a suitable economic solution, although probably unfeasible, would be to collect the efficient award from respondent but only pay claimant the full compensation amount. The outstanding balance could be donated to charity. In this respect, it is observed that any dilatory behavior caused by the level of the PJI rate (or for any other reason, for that matter) "should be [addressed] by separate and evenhanded rules [outside of the issue of pre-judgment interest] thereby preserving the integrity of the law of compensatory damages." J.C. Keir & R.C. Keir, Opportunity Cost: A Measure of Prejudgment Interest, 39 BUS. LAW. 129, 137 (1983).
It has been argued, for example in *Vivendi v. Argentina*,\(^{43}\) that if the award was collected at the time of the breach, it would probably not have produced a return equal to the cost of capital since the company was likely unable to actually earn a return at this level prior to the damaging actions. Although it is true that companies’ returns may be below their cost of capital, it is equally true that, their returns could exceed their cost of capital. In fact, most companies’ returns cannot be systematically below their cost of capital, as otherwise they would not be able to expand, and eventually they would be better off closing down. It is also true that if the company is in a relatively infant stage of its development, it may be experiencing lower returns, but with the expectation of reaping higher returns in the future. The use of the cost of capital, thus, lies in the notion that in competitive markets, firms would be earning on average a return equal to the cost of capital of the industry. Moreover, the linking of the PJI to the cost of capital of the affected business is grounded exclusively in restoring the damaged party to the financial position in which it would have been had it willingly accepted the temporary deprivation of rights but-for the damage (including the delay in collection), and not based on speculative assessments about alternative investment opportunities or on the likely outcome of the reinvestment of the award, within or outside the affected business.

A second concern is the alleged incentives for *claimant* to delay the award decision.\(^{44}\) This argument is based on the rationale that non-financially constrained claimants, who have no investment possibilities available granting such a return, would prefer to “invest” the arbitration proceeds at the PJI by continuous delays.\(^{45}\) We consider this risk to be negligible, or if present, to have only marginal effects, for several reasons. First, tribunals should be able to note and penalize this kind of behavior.

\(^{43}\) See, e.g., Compañía de Aguas del Aconquija SA and Vivendi Universal SA v. Argentina, Award, ICSID Case No ARB/97/3 (Aug 20, 2007) (stating that it “was not convinced that the claimants would have managed to obtain a 9.7% compounded interest on the award had it been collected at the time of expropriation”).

\(^{44}\) See, e.g., Gotanda, * supra* note 1, at 40.

\(^{45}\) Id.
and respondent should object to such tactics as well. Second, respondent has the ability to terminate the interest accrual by paying the damages promptly or even by making pre-payments on account of the award (and without prejudice).

A third concern about the use of the affected business’ cost of capital as PJI is found in the PSEG Global Inc. case, where the tribunal rejected the use of the cost of equity of the affected business as PJI because it “is based on subjective determinations by the investors.” The PSEG Global tribunal held that, given that the cost of equity could be influenced by claimants, it could not be used to compound the value of the expropriation. We agree with the tribunal’s concerns, but do not share its conclusion. The damage calculation process should apply a market-based (generic for the industry) cost of capital as the discount rate, rather than a subjective or claimant-specific rate. A market-based rate will normally be grounded on an optimal capital structure and debt arrangements of the damaged business, to avoid affecting the PJI and all components of the damage quantum by any particular management decisions that could be considered subjective. In sum, our discussion of IRT and full compensation shows that, contrary to the belief that setting PJI at the cost of capital of the affected business is likely to result in over-compensation, this is the rate most likely to guarantee exactly full compensation to claimants.

A. Limitations on the Use of the Cost of Capital as PJI

Professor Gotanda suggests the inclusion of a PJI clause in international contracts to be used in the event of future conflicts. While we agree in principle, the incomplete nature of

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46 In this latter case, as pre-payments will be compounded to the date of award at the same PJI rate as the award is, claimant has no incentive to accept pre-payments in excess of what it considers the value of the award. Moreover, pre-award payments could also foster early settlements.

47 Managers can typically control their company’s level of debt, and, to some extent, the interest rate paid on the debt by choosing among different financial instruments. However, if a company has a capital structure that is inefficient according to the market benchmark, a potential buyer could easily restructure the financing scheme at market prevailing rates.

48 See Gotanda, supra note 1, at 40.
contracts narrows its applicability. Furthermore, certain specific punitive contractual rates (designed to prevent collection delays, for example) cannot be directly applied to all types of breaches not properly specified in the contract. In particular, since contractual interest rates tend to be event-specific, and reflect a specific bargain and risk assignment between the parties, their use for other, unintended purposes should not be adopted blindly.49

The application of the cost of capital as PJI is limited in circumstances under which a business has ceased operations for reasons unrelated to the matter under dispute, relieving claimant from the business risk of the damaged business. For instance, it could be the case that a dispute is related to a concession contract whose original term expired between the date of damages and the date of award.50 In this example, it would be appropriate to recognize PJI at the concession’s cost of capital only up to the pre-agreed date of termination, and at a different rate (ranging from the risk-free rate to the respondent’s cost of debt) thereon. The same would be true in case of a voluntary exit of the industry, for reasons unrelated to the respondent’s allegedly injurious acts.

These examples do not violate the principle of full compensation, however, as the claimant could not have reasonably expected the recognition of the business’ cost of capital beyond the legal termination date or the date of the voluntary early exit, which would have occurred, at the same date, even if the damaging act never occurred. Similarly, such PJI structure does not generate an IRT as the award is granted at a point in time at which no future cash flows related to the affected business exist. It should be noted, however, that this exception applies exclusively to cases where the affected business ceased to

49 Specific interest rates stipulated in a contract are commensurate with the risks and commercial conditions of the transaction to which they refer. For example, if a company is a supplier to a government and the contract specifies a certain late collection interest, it would be unreasonable to apply this same rate as PJI in an eventual expropriation, which involves the deprivation of all of the company’s cash flows, not just those related to the government’s delays in certain payments.

50 A voluntary sale by the claimant decided without consideration for the damaging act is another example.
operate for reasons completely separate from respondent's alleged breach, and should not be applied to cases in which the respondent's actions directly or indirectly caused the business termination, sale or early exit of the business.

VI. CONCLUDING REMARKS

This Article has highlighted, from both the financial and economic perspectives that tribunals frequently err in rendering international arbitration awards by granting PJI at rates lower than the discount rates used to discount cash flows. These PJI rates do not properly account for the risk of the affected business and result in IRTs, in some cases dramatically under-compensating claimants and failing to satisfy the principle of full compensation under international law. By avoiding IRTs, and setting the PJI at the business’ cost of capital, tribunals will, in general, guarantee the principle of full compensation, and foster efficiency in the international dispute resolution system.

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DRAFT REPORT FOR PUBLIC DISCUSSION

OF

THE ICCA-QUEEN MARY TASK FORCE

ON THIRD-PARTY FUNDING IN INTERNATIONAL ARBITRATION

1 SEPTEMBER 2017
ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration

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* In addition to Task Force Members, the Report benefitted from a number of special consultants, who will be acknowledged in the final version of the Report.
About ICCA

The International Council for Commercial Arbitration (ICCA) is a worldwide nongovernmental organization (NGO) devoted to promoting the use and improving the processes of arbitration, conciliation and other forms of resolving international disputes. Its activities include convening biennial international arbitration congresses; sponsoring authoritative dispute resolution publications (including the ICCA Yearbook Commercial Arbitration, International Handbook on Commercial Arbitration and ICCA Congress Series); and promoting the harmonization of arbitration and conciliation rules, laws and standards. ICCA has official status as an NGO recognized by the United Nations. See <www.arbitration-icca.org>.

About Queen Mary

Queen Mary University of London is one of the UK's leading research-focused higher education institutions and one of the biggest University of London colleges. It offers teaching and produces research across a wide range of subjects in the humanities, social sciences, law, medicine and dentistry, and science and engineering, for over 130 years. The School of Law at Queen Mary University of London, where more than 2,000 students study law annually, has been consistently ranked within the top 5 law schools in the UK and the top 35 law schools in the world. <www.qmul.ac.uk>

Any views expressed in this draft Report are those of the Task Force and not those of Queen Mary or ICCA, its Governing Board, or members. Although this draft Report is the result of the collective efforts of the Task Force, the views expressed are not attributable to any particular Member of the Task Force.
This draft Report of the ICCA-Queen Mary Task Force on Third-Party Funding is circulated for the purpose of generating discussion and in order to solicit public comments. The ICCA-Queen Mary Task Force on Third-Party Funding is a joint Task Force established by ICCA and Queen Mary, University of London in 2013.

This draft of the Report, the “Draft Report for Public Comment,” is being published from 1 September through 31 October 2017 for the purpose of obtaining public comment and feedback. After incorporation of such feedback a final version of the Report will be published as a Volume of the ICCA Reports.

The Task Force was composed of a diverse group of leading experts from a wide range of professional backgrounds, including arbitrators, in-house counsel and law firm counsels, members of arbitral institutions, academics, State parties, and a range of funders and brokers. The Task Force is co-chaired by William W. “Rusty” Park, a member of the Governing Board of ICCA, Stavros Brekoulakis, a professor at Queen Mary University of London, and Catherine A. Rogers, also a professor at Queen Mary University of London, and at Penn State Law. The work of the Task Force was coordinated by ICCA Executive Director Lise Bosman and Deputy Executive Director Lisa Bingham.

Preparation of this Draft Report for Public Comment was undertaken by designated individuals who led Sub-Committees to study specific topics. Their work was assisted by the co-chairs and other the Task Force Members. It is based on the work of the Task Force, including discussions at numerous Task Force roundtable meetings over the course of the past three years, related presentations and public discussions, and comments received by Task Force Members and special consultants.

We hope the Draft Report for Public Comment will facilitate robust discussion and submission of concrete feedback through specially organized events, and through submission of comments directly to the Task Force co-chairs at tpftaskforce@arbitration-icca.org.

The final Report of the Task Force will be launched at the ICCA Congress in Sydney in April 2018.
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* During the Public Comment period, the bibliography for the Draft Report for Public Comment will be made available at [http://www.arbitration-icca.org/projects/Third_Party_Funding.html](http://www.arbitration-icca.org/projects/Third_Party_Funding.html).
Chapter 1

Introduction

Modern forms of third-party funding are no longer new to international arbitration.¹ Recent years have seen significant increases in the number of funders, the number of funded cases, the number of law firms working with funders, and the number of reported cases involving issues relating to funding. As a result, third-party funding has increasingly drawn the attention of commentators and scholars, and even more recently of arbitral institutions, national regulatory authorities, and State trade negotiators.

Notwithstanding these trends, many questions remain about the relationship between funding and international arbitration process. To address these questions, in 2013 the International Council for Commercial Arbitration (ICCA) in collaboration with Queen Mary University of London convened a Task Force on Third-Party Funding in International Arbitration. Since its inception, the Task Force has undertaken sustained study and discussion of relevant issues, and its findings are presented in the balance of this Report. This introductory chapter provides an overview of the organization and work of the Task Force.

I. Composition of the Task Force

The Task Force is co-chaired by William W. “Rusty” Park, a member of the Governing Board of ICCA, Stavros Brekoulakis, a professor at Queen Mary University of London, and Catherine A. Rogers, also a professor at Queen Mary University of London, and Penn State Law. The work of the Task Force was coordinated by ICCA Executive Director Lise Bosman and Deputy Executive Director Lisa Bingham.

The Task Force included representation of stakeholders from diverse geographical and industry perspectives. It was composed of over fifty members from over twenty different jurisdictions around the world. The members included arbitrators, in-house counsel, State parties,² external counsel, representatives with experience at arbitral institutions, academics, and a range of third-party funders and brokers. The Task Force first met as a group on 12-13 February 2017, and then on several occasions since then, to engage in substantive roundtable discussions.

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¹ In some sectors, such as maritime, forms of third-party funding have long-existed. In this respect, many of the types of funding addressed in this Report may be regarded as “modern” forms of funding.

² All individuals on the Task Force who are employed by States served on the Task Force in their individual capacity.
These discussions were generally organized around reports on specific topics prepared and presented by individual Task Force Members. Report topics included arbitrator conflicts of interest, costs and security for costs, privilege, and implicated a range of other definitional, policy, and practical issues. The work of the Task Force and this Report also benefitted from extensive consultations with various groups and organizations during this time, and it is hoped will also receive feedback received during a public comment period from 1 September through 31 October 2017, both through individual comments and through the numerous roundtable discussions and public symposia that are organized during that period.3

II. Task Force Objectives

The Task Force’s objectives emerged out of its work. No specific work product was initially envisaged and no specific mandate explicated. Its starting objective was to identify and study the issues that arise in relation to third-party funding in international arbitration, and to determine what outputs, if any, would be appropriate to address them.

Initially, views of Task Force members largely reflected the range of perspectives that had been publicly expressed. Some were generally disinclined to produce any form of prescriptive guidance, both for substantive reasons (examined in greater detail below) and in light of what some regard as an excess of “para-regulatory” or soft law instruments in international arbitration.4 Others believed that the Task Force should aim to produce for international arbitration a code of conduct for third-party funders, similar to the Litigation Funders Code in England and Wales, or other form of regulation.

Despite these initial differences, the Task Force quickly identified two questions on which members of the Task Force agreed. First, members agreed that all stakeholders would benefit from greater understanding about what third-party funding is and from multi-lateral dialogue about the issues it raises in international arbitration. From this observation, one of the Task Force’s primary objectives emerged: to facilitate education and informed dialogue.

Second, members agreed that stakeholders would benefit from greater consistency and more informed decision-making in addressing issues relating to third-party funding.5

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3 A list of events at which the Task Force’s work and drafts have been or will be presented can be found at http://www.arbitration-icca.org/projects/Third_Party_Funding.html.

4 See generally Daniele Favalli (ed.), The Sense and Non-sense of Guidelines, Rules, and other Para-regulatory Texts, International Arbitration, ASA Special Series NO. 37 (Juris 2015); but see Queen Mary Survey, (finding an overall positive perception of guidelines and soft law instruments, with only 31% responding either that they were too numerous or not useful) Queen Mary University of London and White & Case, “2015 International Arbitration Survey: Improvements and Innovations in International Arbitration” (2015) available at <http://www.arbitration.qmul.ac.uk/docs/164761.pdf> (last accessed 21 August 2017).

challenge, of course, is that however desirable consistency may be in the abstract, disagreement remains—both on the Task Force and beyond—about how and on what terms such consistency should be achieved.

In both public debates and on the Task Force, debate has largely moved beyond questions about whether third-party funding should be permitted, to evaluation of more specific issues that are implicated by third-party funding.6 Divergent perspectives on these issues remain, however, and in turn affect how differently situated stakeholders view the appropriate means and standards for achieving consistency. The Task Force began its work cognizant of the tensions among a need for consistency, the continued and evolving debate about third-party funding, and (as discussed in greater detail below) the rapid pace of evolution both in international arbitration practice and the funding market. Against the backdrop of these tensions, the Task Force began its work by identifying the most frequently occurring issues that arise in relation to third-party funding in international arbitration.

Since the Task Force was initially constituted in 2013, there have been several important developments relating to third-party funding. The funding market has expanded in several respects. The number of cases funded has increased significantly. The number and geographic diversity of funders has also increased, with new entities continuing to enter the market and consequently increase the aggregate amounts available for funding. Perhaps most importantly, the forms of dispute financing have expanded significantly, raising challenging questions about how “third-party funding” should be defined.

Other developments involve changes in the regulation of third-party funding. Just in the year prior to publication of this Report, prohibitions against funding international arbitrations have been relaxed or eliminated in some important jurisdictions, most notably Hong Kong and Singapore. In conjunction with relaxing prohibitions against funding in international arbitration, these jurisdictions also introduced new regulations, most importantly with respect to disclosure for costs is certainty. We simply want to know when and on what bases we will be liable to pay these amounts.”); Van Boom (“In investment arbitration, the parties do not have certainty at the beginning of proceedings if, and to what extent, the English or American rule will be applied concerning cost-shifting. This probably renders it unappealing for TPF funders to voluntarily disclose their involvement.”); see also William H. VAN BOOM, “Third Party Financing in International Investment Arbitration”, (21 December 2011) p. 50, available at: <http://poseidon01.ssrn.com/delivery.php?ID=4271000070710030980241240250831070860600330641010905011108114103076068007111081120120049058116059030048032000068124093071102509705083035032000084076067101091115100027052023101090100089027068021072067103072109082097092106073088066081107104125023098092> (last accessed 27 October 2016).

6 As one commentator explains:
“Whether in favor or against TPF, the industry is increasingly requiring a clear, uniform and binding regulatory framework within the field of international arbitration. This is confirmed by the results of the 2015 Queen Mary School of International Arbitration survey where a clear majority of practitioners (71%) expressed a desire for regulating the industry, and approximately half of respondents (49%) with practical experience in TPF agreed with the findings.”
the purpose of assessing arbitrator conflicts of interest. At the same time, other international bodies also introduced new obligations, particularly with relation to disclosure.7

Another, more amorphous development is that in recent years the poles of the debate over third-party funding appear to have moderated somewhat.8 When the Task Force started, it was more common to hear, at least among some funders, that funding is essentially just a form of corporate finance, which should not be subject to any regulation other than what already exists within financial markets.9 By contrast, particularly in the international investment context, there were arguments to eliminate third-party funding because of its asserted consequences for the real and perceived legitimacy of investment arbitration.10

A number of reasons explain why some of the more extreme positions are not asserted as often or with as much vigour. First, third-party funding has also become available to and has been used by State parties in investment arbitration, and in some cases it has provided access to justice that a legitimately aggrieved party would not have been able to bring. These developments have made it more difficult to fundamentally reject the practice altogether. It is also now more generally recognized by both supporters and detractors that, in a globalized market for legal services and among arbitration providers, third-party funding is here to stay.

Modern forms of funding are also now recognized as resembling in essential ways certain alternative types of funding that have long-existed and are more widely accepted, such as contingency and conditional fee arrangements and insurance.11 These similarities can make it difficult to draw distinctions that would be a basis for limiting or precluding third-party funding, and these difficulties are in turn complicated by the challenges in regulating the legal

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7 For a discussion of international investment treaties and agreements that address third-party funding, see Chapter 4, at p. 48.
8 As one article described, at one end of the spectrum third-party funding was regarded as the “arbitration antichrist,” while at the other end it was regarded as “the best thing since sliced bread.” Sebastian PERRY, “Third-Party Funding: The Best Thing Since Sliced Bread?”, GAR (28 November 2012) (reporting on GAR Live London debate) available at <http://globalarbitrationreview.com/news/article/31006/third-party-funding-best-thing-sliced-bread> (last accessed 27 August 2017).
representation of parties in international proceedings. For proponents and opponents of funding, therefore, it is now generally accepted that funding will be part of the modern reality in international arbitration.

Finally, the international arbitration community has focused on finding solutions to the high cost of arbitration. Funding is increasingly regarded as a potential solution to this problem, both in investment arbitration and beyond.

As a consequence of these developments, both the public attention and the Task Force inquiries have largely focused on more nuanced questions: 1) what issues does funding raise in international arbitration?, and 2) how should those issues be addressed? The premise for the Task Force was that answers to these questions would best be developed through active dialogue that involves a full range of perspectives and takes account of all stakeholder interests.

III. The Scope of the Task Force’s Work

Third-party funding raises a number of potential issues. The Task Force, however, limited its work to those issues that: (1) directly affect international arbitration proceedings; and, (2) are capable of being addressed at an international level. This focus leaves many important issues outside the scope of the Task Force’s work and this Report.

For example, the Task Force did not address several more technical issues relating to financial markets and issues that are generally addressed through lawyer ethics and regulation at the national level. For this reason, the Report does not address specifically lawyers’ obligations to clients with respect to third-party funding arrangements. Many systems impose, through professional regulation or otherwise, obligations or prohibitions on attorney conduct that apply when a client is funded.12

Those rules and regulations are not generally implicated in arbitral proceedings, and there is no international consensus about the reasons for and against them. Moreover, some efforts to regulate third-party funding relate to issues such as whether a funder is adequately capitalized,13 an issue not directly implicated in international arbitral proceedings. For these reasons, the Task Force and the Report do not directly address these issues.14

In addition, for some, questions remain about how third-party funding affects larger policy issues like the extent to which it actually affects access to justice and whether it may impact the

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12 For example, in the United States, attorney codes of ethics have express rules regarding an attorney’s duty of loyalty when a third-party is paying the client’s fees. Meanwhile, many jurisdictions still prohibit contingency fee arrangements, which are often part of a third-party funding agreement.
14 For these reasons, this Report does not seek to propose “regulation” of third-party funding, as that term is generally understood. Instead, it seeks to provide limited guidance on select key issues.
number of cases brought or be used for strategic purposes. These are important questions, and it is hoped that this Report may facilitate discussion and debate about these larger policy issues. To that end, the Report often articulates competing policy arguments that were raised in or implicated by Task Force discussions.

Notably, the inclusion of references to such policy issues drew concern during the drafting process. Policy debates over funding have sometimes included harsh characterizations of funding that are regarded as unfair. On the other hand, economic and market-based analysis of issues regarding funding are sometimes regarded as improperly diminishing issues about legitimacy. In the drafting process, reference to either side of these policy debates sometimes drew concern that the Report was endorsing or legitimating a particular side of the debate. These concerns were especially acute in discussions regarding investment arbitration cases and in Chapter Eight, which provides an overview of policy debates in investment arbitration.

Given its narrow focus on issues that directly affect international arbitral proceedings, and particularly the absence of relevant empirical research, the Report does not aim to resolve these larger policy issues, but only to include reference to them where relevant for context. In this respect, Chapter Eight provides an independent outline of the policy issues, but again mostly to amplify the policy issues raised in earlier chapters and provide a basis for future discussion.

Another important limitation on the work of the Task Force is that it explicitly carves out maritime arbitration from the scope of the recommendations in this Report. At least according to some definitions, third-party funding has long existed in maritime arbitration through membership clubs that provide Protection and Indemnity (“P&I”) insurance and Freight, Demurrage and Defence (“FD&D”). The existence of membership clubs, and the fact that maritime arbitration is a distinct field that has distinctive internal rules, specialized arbitral institutions, a specialized body of practitioners, and a well-established history of funding maritime disputes, put the topic of funding in maritime cases beyond the scope of the Task Force’s inquiry and outside of its recommendations.15

To date, most efforts to regulate third-party funding, which focus on more modern forms of funding, do not appear to have contemplated specifically their effect on maritime arbitration and the funding regime that has long existed in that field. For these reasons, even though funding in maritime arbitration might presumptively fit within the Working Definition of third-party funding in this Report, it is expressly carved out from the definitions used in this Report. To the extent it is occasionally mentioned, the reference is only as a point of comparison.

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15 See Chapter 1, at p. 6. The term “maritime arbitration” refers to the range of arbitration disputes that arise out of circumstances between parties engaged in maritime affairs, and/or to arbitrations brought pursuant to maritime arbitration rules, such as those of the London Maritime Arbitration Association. P&I and FD&D are referred to in Chapters 2, 3, and 6 simply as a point of historical reference. Although maritime arbitration is specifically identified in this carve out, the recommendations of this Report may also be inapposite for other forms of ad hoc and trade association arbitration, where more traditional forms of funding is the norm.
IV. Organization and Structure of the Report

In terms of the format, each of the main substantive chapters of this Report begins by articulating specific Principles for each of the topics it covers. The Principles from these substantive chapters are collected in a comprehensive whole as an Annex to the Report, and may be referred to collectively as ICCA-Queen Mary Principles on Third-Party Funding (the “ICCA-Queen Mary Principles” or “Principles”).

The body of each of these chapters provides a detailed analysis of the sources and competing viewpoints the Task Force considered in reaching these Principles, as well as the reasons why particular viewpoints were eventually incorporated into the Principles instead of others. Beyond the guidance provided by the Principles, the substantive analysis will be useful for future consideration of the relevant issues, particularly in light of future developments that may prompt reconsideration of the Principles themselves.

In terms of the structure of the Report, after this Introduction, Chapter Two provides an overview of the market and mechanics of third-party funding. It begins with an examination of the reasons parties seek funding, and the process funders use to evaluate whether to fund a dispute. It then provides a descriptive overview of the range of means for financing disputes, including both modern case-specific non-recourse funding and a range of other sources that serve similar functions.

Building on Chapter Two’s overview of the forms of funding, Chapter Three then examines the definition of third-party funding. Specifically, Chapter Three provides a broad working definition and examines different possible definitions, surveys the range of definitions that have been adopted by various other sources, and concludes by examining how different definitions affect analysis of different issues addressed in subsequent chapters.

Importantly, as elaborated in Chapter Three, this Report and its recommendations do not extend to maritime arbitration and the forms funding that exist in that field. Many definitions of third-party funding, including the Working Definition in this Report, would ostensibly apply to traditional modes of funding in maritime arbitration. However, funding in the maritime context exists within a historical tradition and subject to a set of existing practices and internal norms that were beyond the scope of the Task Force’s work.

Each of the substantive chapters of this Report begins by articulating specific Principles for each of the following topics: Disclosure and Conflicts of Interest (Chapter 4), Privilege (Chapter 5), and Costs and Security for Costs (Chapter 6). The Principles from these substantive chapters are collected in a comprehensive whole in Chapter Seven, and may be referred to collectively as ICCA-Queen Mary Principles on Third-Party Funding (the “ICCA-Queen Mary Principles” or “Principles”).
The body of each of these chapters provides the sources and competing viewpoints the Task Force considered in reaching these Principles, as well as the reasons why particular viewpoints were eventually incorporated into the Principles instead of others.

Chapter Four addresses the issue of disclosure and potential arbitrator conflicts of interest. Consistent with other recent sources, the principle it articulates requires disclosure of the existence and identity of third-party funders to facilitate analysis of potential conflicts. In its current form, this Report includes proposed alternative versions of the Principles regarding disclosure in order to facilitate specific input regarding those issues for which there was disagreement on the Task Force.

Chapter Five addresses privilege. It provides a survey of national differences regarding privilege, which is supported by an Annex that collects national reports indicating how different jurisdictions treat it articulates an international principle regarding waiver of information that is otherwise determined to be subject to privilege. Specifically, it recommends that tribunals do not treat privilege as waived by virtue of information being shared with a third-party funder.

Chapter Six takes up the issue of costs and security for costs. It analyzes existing standards for granting costs and security for costs, concluding that the existence of funding is not generally relevant to such determinations.

Chapter Seven summarizes best practices for funding agreements. Task Force members generally agreed that a statement of existing best practices would be useful to new parties seeking funding, new funders entering the market, and the increasing number of arbitrators and counsel that are encountering funding for the first time.

Finally, Chapter Eight examines third-party funding in investment arbitration. The analysis in each of the foregoing chapters also analyzes the relevant issues in the context of investment arbitration. This Chapter, however, seeks to provide additional analysis of both the policy issues that affect how the Principles of this Report are applied in investment arbitration, and a limited range of specialized issues that arise with respect to funding in investment arbitration.

V. Conclusion

At least in theory, parties could adopt the ICCA-Queen Mary Principles to govern their proceedings. More likely, and more consistent with the intent of the Task Force, parties, counsel, and arbitrators may reference or invoke the Principles to address issues that arise in the course of an arbitration, in entering into a funding agreement, and in continued discussions and debates regarding third-party funding.16 The Report may also be useful for national courts in reviewing

16 The Principles have been drafted to reflect existing norms and emerging trends. To that end, it is not anticipated that they would be applied retroactively, though they may provide guidance for cases that have already been commenced.
international arbitral awards or in satellite litigation, and for regulatory bodies and arbitral institutions that seek to address issues relating to third-party funding in international arbitration.

Particularly in light of how rapidly international arbitration practice and funding models are evolving, this Report does not aim to be either definitive or permanent. Changes in the field and considerations that arise within in particular regulatory contexts may require reconsideration of, or readjustment to, the Report’s Principles and amplification of its analysis. While this Report will not be the last word on issues relating to third-party funding, it develops an important set of conceptual frameworks and detailed analysis that the Task Force hopes will provide a foundation for future work in the area.
Chapter 2†
Overview of Dispute Funding

I. Dispute Funding: An Introductory Overview

As international arbitration continues to grow in prominence and complexity, so do the attendant costs and demands from users of the process to find innovative ways to finance their matters.17 “Whether in favour or against, third-party funding of litigation and, more recently, arbitration, is an undeniable and important reality.”18 Anecdotal reports suggest that the global market for dispute funding is in the billions, likely currently exceeding USD $4 Billion and is growing.19

The business of law is changing and dispute funding is very much an integral part of the future of the global arbitration and litigation markets. It is amidst this backdrop that an exploration of the interplay between dispute funding and international arbitration is not only increasingly timely, but of the utmost importance. The arbitration community must find a way to balance the increasing business need for innovative approaches to the financing of legal matters while protecting the integrity of the arbitral process and the ultimate enforceability of awards. The aim of this chapter is to provide a general overview of dispute funding as it relates to international commercial and investment arbitration.

A. What is Dispute Funding?

In less than a decade, dispute funding has moved from the fringes of a handful of common law jurisdictions to centre stage in the global commercial litigation and arbitration market. Dispute funding first started in Australia and then migrated to the United Kingdom in the beginning of the

† This Chapter was authored by James Blick and Erika Levin, with input from other Members of the Task Force.

In its simplest form, third-party funding involves an entity, with no prior interest in the legal dispute providing financing to one of the parties (usually the claimant). Typically, this financing is offered on a ‘non-recourse’ basis, meaning that the funder has no recourse against the funded party if the case is unsuccessful. The funder’s recourse for repayment of the capital advanced and return on the capital invested is limited only to the claim proceeds recovered, if any.

i. Rising Demand for Funding

It has been suggested that the rapid expansion of this type of funding was fuelled by the economic downturn in 2008. Many corporations and investors experienced economic instability and were unable to proceed with meritorious claims due to reduced cash flow. At the same time, investors were seeking alternative capital outlets, where returns would not be correlated to traditional markets. It remains to be shown, however, that there is any real as opposed to coincidental correlation between the 2008 crisis and the expansion of third-party funding in international arbitration.

In recent years, with the rising costs of international arbitrations and the additional number of constraints being placed upon corporate legal budgets, it is not surprising that the demand for dispute funding has continued to increase. According to Professors Sahani and Nieuwveld, the “three main forces driving the sharp increase in the demand … [are: (1)] increasing access to justice … [; (2)] companies seeking a means to pursue a meritorious claim while also maintaining enough cash flow to continue conducting business as usual … [; and (3)] worldwide

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21 See VON GOELER, supra at 2, p. 1, n. 1 (citing CIArb Costs of International Arbitration Survey 2011, 13 (survey of 254 international commercial arbitrations conducted between 1991 and 2010 finding that claimants on average spend GPB 1,580,000 in total, while respondents spend GPB 1,413,000); UNCTAD, Investor–State Disputes, 16-18 (‘[c]ontrary to the expectations, it turns out that costs involved in investor–state arbitration have skyrocketed in recent years … costs for conducting arbitration procedures are extremely high’) (emphasis original); OECD, Government Perspectives on Investor-State Dispute Settlement, 8 (‘legal and arbitration costs for the parties in recent ISDS [investor-state dispute settlement] cases have averaged over USD 8 million’)).
market turmoil and uncertainty … which has inspired .. investors to seek investments that are not
directly tied to or affected by the volatile and unpredictable financial markets.”22

“The global economic slowdown has also inspired companies facing bankruptcy or insolvency to seek funding to pursue claims that may generate cash flow for their businesses or mitigate the risk of losing a 'bet-the-company' dispute.”23 Additionally, and not surprisingly, the aforementioned economic situation has increased client pressures upon law firms to deliver innovative solutions, some of which require the use of funding directly by the law firms in conjunction with the offering of alternative fee arrangements, in order to attract legal work.24

Rising demand for third-party funding has now led to a boom in supply. The last few years have seen numerous newentrants into the global dispute financing market, in addition to which many of the larger, established players are continually raising new capital and the growth of the industry shows no signs of slowing.

**ii. Why is Funding Sought and by Whom?**

The key participants in the dispute funding process are the claim holders, funders, lawyers and, potentially, funding brokers. Funding may be sought to cover legal fees, out-of-pocket costs (e.g., expert fees, arbitrator fees, arbitral institution fees, discovery-related fees, etc...), or costs associated with subsequent enforcement actions or appeals and may be structured around a single claim or a portfolio of claims. Dispute finance is also increasingly being used by claim holders for other purposes, such as for example raising working capital for the claimant entity, discharging other financial liabilities or financing other litigation (unrelated to the claim against which the finance is secured).

Historically third-party funding was often considered as being primarily relevant to financially distressed claimants as a way of obtaining access to justice. However, much of the focus of the litigation finance market today is on the growing corporate utilization of funding by large, well-resourced entities, who are looking for ways to manage risk, reduce legal budgets or take the cost of pursuing arbitration off-balance sheet, or other business reasons for not wanting to...

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22 Victoria SHANNON SAHANI and Lisa Bench NIEUWVELD, Third-Party Funding in International Arbitration, (Kluwer Law International 2012) p. 12. See also, Christopher P. BOGART, Chapter 4. Overview of Arbitration Finance, in Bernardo M. CREMADES SANZ-PASTOR and Antonias DIMOLITSA (eds), Third-Party Funding in International Arbitration (ICC Dossier), Dossiers of the ICC Institute of World Business Law, Volume 10 (Kluwer Law International; International Chamber of Commerce (ICC) 2013) p. 51 (“Litigation and arbitration, particularly investor-state arbitration, are unduly expensive and frequently inefficient, and those deficiencies interfere with their ability to deliver justice.”).

23 SAHANI, at p. 12.

24 See Nick ROWLES-DAVIES, Third Party Litigation Funding (Oxford: Oxford University Press 2014), p. 61 [3.08] (Lawyers “are having to be innovative to survive …. The economic climate since the ‘Great Recession’ which began in around 2008 has caused many, even traditional institutional clients, to look for ways to reduce their legal fees, along with their business costs.”)
allocate resources to financing an arbitration matter.\textsuperscript{25} Put simply, funding is not only for those that are impecunious. “The use of funding offers the client the ability to minimize risk, does not have any negative effect on their cash flow, and ensures payment of lawyers.”\textsuperscript{26}

1. Claimants

As noted above, the vast majority of recipients of third-party funding are claimants. At one end of the spectrum, there may be a party that has invested all of its resources into a failed project and funding provides this investor with the only mechanism by which the investor can seek redress from the parties that caused its losses.

Somewhere in the middle, exists a claimant, who may be adequately capitalized, but nonetheless is a smaller entity than the corporation it wishes to pursue an action against. In his book, Nick Rowles-Davies provides an example that captures this scenario well.\textsuperscript{27} The example involves a mid-size company that has been wronged by a much larger competitor and is faced with the decision of whether to spend its capital on vindicating its rights (and unlocking a potential recovery) or allocating those resources to its core business operations.\textsuperscript{28} In addition, even if it does decide to self-fund the matter, it is likely that it will be outmatched in resources by its opponent. But for funding, the claimant would be in an untenable position. Funding allows the claimant to grow its business while pursuing the action in a manner that poses no cash flow burden or risk.\textsuperscript{29}

At the other end of the spectrum, large corporations with strong balance sheets are increasingly employing dispute funding as a corporate finance tool that allows them to effectively manage their disputes without negatively impacting their balance sheets.\textsuperscript{30} Dispute funding for corporate clients can take on a variety of forms including traditional capital outlay by funders as well as insurance/hedge offerings, which enable clients with good liquidity to mitigate litigation risk without paying substantial returns to a third-party funder.\textsuperscript{31} As an alternative to tying up their

\textsuperscript{25} See BOGART, at p. 51 (Dispute funding “has developed quickly because it allows corporations to unlock the often substantial value they have tied up on unresolved claims and because it allows them to proceed with arbitrations while retaining control of their exposure to loss.”)

\textsuperscript{26} See ROWLES-DAVIES, at p. 62.

\textsuperscript{27} See ROWLES-DAVIES, pp. 63-64 (highlighting a “real life practical example of a mid-sized company deciding whether to embark on a piece of litigation … [against] a much larger competitor.”)

\textsuperscript{28} Id.

\textsuperscript{29} Id. at 63.

\textsuperscript{30} “Litigation can be financed – just like any other corporate expense. Yet most corporations still pay for legal costs out of pocket, and that has a profoundly negative financial impact: reducing operating profits, impacting publicly reported earnings, and thus valuation. Litigation finance removes this problem by shifting the cost and risk of pursuing high-value litigation off corporate balance sheets.” http://www.burfordcapital.com/what-we-do/for-businesses/ (last visited, 14 August 2017).

own capital in litigation or arbitration, corporations can use dispute funding to pursue arbitrations that can help transition their in-house legal departments from cost centres to profit centres.

2. Law Firms

The role played by law firms in the third-party funding market is a multi-faceted and evolving one. In some instances, law firms, themselves, may be the users of dispute finance. For example, a law firm could seek the use of third-party funding as a way to support contingency fee opportunities, as discussed more fully below. In this context, the law firm would approach the funding market directly in order to seek financing options for its own fee risk exposure and enhance its ability to offer alternative billing offerings relative to its competitors.

As discussed more fully below, in some instances a law firm may effectively act as the provider of dispute finance, for example when offering to act on a contingency fee basis.

Even where not directly a party to the funding agreement, the law firm’s role is often pivotal in a claimant’s decision as to whether it should explore the possibility of third-party funding and the approach taken if funding is sought. Although awareness of litigation finance is rising amongst corporate counsel, most claimants rely heavily on their legal advisors for advice relating to third-party funding, the costs and practicalities involved, and which funder(s) or broker should be approached. Funders therefore cultivate relationships with law firms in order to encourage future referrals. In some instances, even where a law firm is not a direct party to the eventual funding agreement, the firm may still be highly invested in the outcome of the approach to funders. It is not uncommon for a law firm acting for a financially distressed client to invest significant time on a speculative basis in preparing a case for presentation to funders, understanding that it will only be able to recoup that time investment if funding is successfully obtained.

While the majority of opportunities presented to the funding market come via law firms, a growing awareness of third-party funding amongst clients has led to an increased percentage of claimants seeking funding directly, often prior to selecting a law firm (e.g., while still engaging in a law firm tender process).

3. Brokers and other intermediaries

As an alternative to approaching the funding market directly, some lawyers and claimants opt to use the services of a specialist third-party funding broker to advise on potential financing options, access a broader range of funders and manage the process. With the ever-growing number of funds operating worldwide, as well as the range of alternative insurance structures available,

32 See Burford Capital article, at p.15.
brokers play an increasingly prominent role in the process of sourcing and structuring dispute finance arrangements.

4. Respondents

While far from commonplace, the current availability of financing for respondents is evolving. Putting aside scenarios where a party may be defending a claim, but either via a counterclaim or a successful defence of the arbitration could unlock a significant financial upside, the funding of respondents is still quite rare. Outside of the above scenario, the challenge is how to remunerate the funder for the provision of capital in the event of successful defence, while avoiding potential moral hazards created by the existence of the funding. A theoretical option for respondents in situations where they can value their exposure may be to identify a realistic exit point, which if met, will trigger a payment of some amount to their funders or law firms. Essentially, this would translate into a payment by the respondent to the funder for some amalgamation of “the amount by which its liability has been reduced, comparing the amount originally claimed with the amount awarded”. While this structure is from time to time described in theory, in reality there appear to have been few such arrangements successfully negotiated between funders and respondents. A rare example is to be found for instance in *RSM Production Corporation v Grenada*, where the Respondent State was funded by a third party.35

Occasionally, cause-based funding of a defendant has occurred (e.g., Philip Morris v. Uruguay, ICSID case no. ARB/10/7). As noted in following sections, the defence of a claim could also potentially be included in a portfolio arrangement.

B. The Dispute Funding Process

i. Fundamentals

The nature, structure, and features of third-party funding arrangements can vary significantly from case to case, as can the process involved in putting the arrangement in place. It

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33 In scenarios like this, a funder could agree to defend the respondent in exchange for a percentage of the proceeds and/or market share that are unlocked as a result of winning the case.

34 VON GOELER, *supra* at 2, pp. 48-49.

35 Jean-Christophe HONLET, *Recent decisions on third-party funding in investment arbitration*, ICSID Review (Fall 2015) 30 (3): 699-712, at fn 30 doi: 10.1093/icsidreview/siv035. It appears from a separate decision in a subsequent case that such third party was a company called ‘Global Petroleum’. See, Rachel S. Grynberg, Stephen M. Grynberg, Miriam. S. Grynberg and *RSM Production Corporation v. Grenada*, ICSID Case No. ARB 10/6, Tribunal’s Decision on Respondent’s Application for Security for Costs (14 October 2010) para. 4.5. Global Petroleum had been awarded the oil exploration rights lost by RSM Production Corporation in Grenada and saw an interest in having the State prevail in the arbitration. See also Investment Treaty News (28 April 2010).
may surprise some that the vast majority of cases presented to any given funder are rejected by the funder for one reason or another. There are few published statistics available, however anecdotal reports, as well as statements made by some funders, suggest rejection rates of 90% or higher, although this may change with the growing number of funders entering the market, coupled with the increasing familiarity amongst lawyers and their clients with the basic requirements of most funders.

The decision as to whether or not to support a claim will be taken following detailed due diligence by the funder, (often using external counsel, and potentially damages or technical experts) and approval by the funder’s board or investment committee. Funders are primarily concerned with the case merits, the economics of the proposed investment (i.e., the ratio of the legal costs budget to the realistic claim value, which will dictate the level of return the funder may be able to achieve), and the enforceability of any award.

In order for a funder to seriously consider a potential opportunity, there must be an adequate demonstration of a solid claim with a healthy, recoverable margin between the anticipated damages recovery and budget expected for legal fees and costs. The facts, the merits, the parties, and their representatives will all play a crucial role in this calculus. “In addition, the analysis will consider other factors such as: 1) value of the law suits; 2) amount to be advanced; 3) jurisdictional obstacles; 4) defences; 5) nature and length of the proceeding (including whether arbitration or litigation; venue and applicable rules); 6) possibilities of settlement; 7) creditworthiness of client and the opposing party (particularly with a view to collection prospects); 8) counsel chosen and compensation structure (whether there is a contingency fee agreement in place) or 9) additional obligations of the party to be funded linked to the potential risk of recovery (such as previous funding agreements or any other alliance).”

1. Economics

By far the most common reason for a potential opportunity being turned down by a funder is not concerns over the legal merits of the case, but rather concerns that the quantum of the claim (or at least the realistic recovery or likely settlement value) will not be sufficient to justify the level of investment required in order to finance the arbitration budget.

Few funders will wish to embark upon a case where the most likely outcome will see the combined funding costs (reimbursement of funder’s capital and success fee, any contingent litigation insurance premium payable and any contingent fee payment to the legal team) leaving the claim holder with a minority share in the recovery. While funders’ approaches to this issue

vary, many will include a fairly crude economics test in their investment criteria, requiring a minimum ratio between the funding request and a realistic claim value of 1:10. It may be assumed that these numbers will leave a sufficient margin to allow for the claim holder to retain more than half of the claim proceeds, after deducting the cost of the funding arrangement.

Most funders tend to be highly conservative when valuing claims and will concentrate on the realistic or likely “floor” value of the claim - - as opposed to the maximum potential (but inherently more speculative) claim value.

Funders will also carefully scrutinize the arbitration budget (assuming that the financing is being provided primarily or solely for this purpose). A light or overly optimistic budget may be a cause for concern. While the funding commitment will be limited to a fixed or staged sum, a case which exceeds the budget where there is no pre-agreed mechanism in place to deal with the overrun can be problematic for all parties, potentially necessitating renegotiation of the funding agreement mid-way through the case. Funders increasingly will address this issue upfront, potentially requesting a fee cap or an overrun agreement from the claimant’s legal team in order to secure budget certainty.

Ultimately, the most desirable cases are those that have a very high (realistic) claim value as well as a high ratio between the arbitration budget and the quantum of the claim.

2. Return Structures

A dispute funder providing “non-recourse” litigation finance will generally expect to make a multiple return on the capital invested. This reflects both the high-risk nature of the investment as well as the Internal Rate of Return (“IRR”) expectations of those that invest in litigation funds. From the claimant’s perspective, the funder’s return (or success fee) may be structured in a number of different ways. It may be structured as a multiple of the capital invested or as a percentage of the ‘claim proceeds’ (the amount recovered by way of damages or settlement). Some arrangements will involve a combination of these, for example the greater of 3x the capital invested or 35% of the claimant’s recovery. By way of illustration, this was the structure and pricing of the funder’s return in the Norscott v Essar case, in which the arbitrator heard and accepted evidence from James Blick of The Judge Limited that the cost of the funding was reasonable in the circumstances of the specific case in question.37

It is also common for the funding agreement to link the funder’s return to the duration of the case (or to the amount of capital drawn down), meaning that the funder’s return is lower if the case settles early, but rises throughout the proceedings. Such a structure will facilitate early

37 Sir Philip Otton sitting as a sole arbitrator in an arbitration subject to the International Chamber of Commerce (ICC) rules made the unusual award that the Respondent should be liable for the cost of the claimant’s funding arrangement, in addition to the damages awarded. Essar applied to the English Court to have the award set aside under s. 68(1) of the Act on the ground of serious irregularity, but was unsuccessful in its application.
settlement for the claimant, while ensuring that the return to the funder is more proportionate to the actual capital risk taken if the case settles early.

While many funders target broadly similar returns, the differences from a claimant’s perspective between different funding offers on a specific matter can be huge, especially where the claim value is high. Fully understanding the commercial terms of any funding arrangement requires, at a minimum, some basic financial modelling in order to calculate the amount that the funder will be entitled to in a range of theoretical settlement outcomes at different stages of the case with different levels of capital deployed. With the growing number of funders competing for business, claimants are well-advised to obtain and compare (either via brokers or directly) multiple funding offers before entering into a funding agreement.

3. Waterfall

Closely related to the funder’s return structure is the waterfall agreement or priority agreement. This will either be contained in the funding agreement or in a separate document and will usually require execution by all “stakeholders”, *i.e.*, those entitled to a share or contingent payment from any recovery, typically including the claim holder, the funder, the law firm and any insurer providing coverage for fees, costs or an adverse costs award. The waterfall will set out how the claim proceeds are to be divided between the stakeholders and can be as important as the return structure when considering the cost of a potential financing arrangement.

4. Risk Alignment

Risk alignment (or “skin in the game” as it is more colloquially referred to) is an important consideration to many funders when considering a potential opportunity. Some funders have a strict requirement that the law firm should assume some element of risk in relation to its fee budget, either by offering a partial contingency fee and/or fee cap or overrun agreement. Even for those funders that do not require this as a matter of course, a law firm’s (and/or client’s) willingness to share in the risk and reward will be seen as a positive feature when assessing a potential funding opportunity.

5. Control

The extent to which the funder will take over control of the arbitration and the claimant’s decision-making process (*e.g.*, whether, when and at what level to settle the claim) is often a concern expressed by claimants, lawyers and regulators, as well as an important issue in
considering the legality of the financing arrangement in common law jurisdictions where doctrines of maintenance and champerty still exist.

In reality, the vast majority of third-party funding arrangements are structured carefully to ensure that the funder does not have control over the case or the claimant. In many jurisdictions, this is essential in order to avoid or minimize the risk of a challenge to the lawfulness of the funding agreement. Even in civil law jurisdictions which permit the sale or assignment of claims, many funders still adopt this common law model, although there are also many examples of funds in such jurisdictions seeking to purchase and aggregate (and thus take over control of) claims. This is prevalent, for example, in cartel damages claims in jurisdictions such as Germany and the Netherlands, but less common in international arbitration.

However, even where the funding arrangement does not seek control, there are nevertheless certain safeguards built in to protect the funder’s investment. A third-party funding arrangement is not an unconditional agreement to fund the case to conclusion. Provision of ongoing funding will be subject to the merits of the case and compliance with the terms of the funding arrangement. Breach of the agreement or a fundamental change in the likelihood of success may entitle the funder to terminate the agreement (and, in some instances of serious breach, may allow the funder to seek recourse for the amount invested). While this does not amount to direct control, if the claimant is financially reliant upon the funder in order to purse the claim to conclusion, the possibility of the withdrawal of funding may still amount to powerful indirect control.

Related to the issue of control is the question of how actively the funder wishes to monitor its investment. This varies from funder to funder, but it should be assumed that at a minimum, the funder will require reports about the progress of the case, notification of any significant developments (e.g., settlement offers or new information which changes the case outlook) and direct access to the claimant’s legal team. In some instances, the funder may play a highly active role, attending client meetings and/or hearings, being copied on correspondence and having input on strategic issues. Some clients may see this active involvement by the funder as an additional ‘value add’ in terms of legal, strategic or technical expertise, beyond the mere provision of capital.

6. Confidentiality / Privilege

Securing funding necessarily requires the sharing of confidential, privileged and on occasion highly sensitive information with prospective funders. Ensuring that the confidentiality of such information is protected (to the same standards) and that the privilege is not lost is an important issue that claim holders and their advisors must consider before seeking funding.

Anyone navigating the process must balance the disclosure of information required for assessment/due diligence and minimizing the risk of waiving privilege. Certain basic steps, such as entering into non-disclosure agreements before sharing any information and limiting the information shared early on, are fairly standard practice, however the concerns and protocols will
necessarily vary depending on the jurisdiction involved. In some jurisdictions, the law is fairly well-established, whereas in others it is still evolving (although generally in the direction of accepting that parties should be able to share information with funders without waiving privilege). 38

Attempts to address the calls for greater transparency with respect to the disclosure of the existence of funding arrangements must take note of what will occur post-disclosure. Depending on the jurisdiction involved, the disclosure of the existence of a funding relationship could have very different results. On the one hand, in a civil jurisdiction where discovery is not readily available, the disclosure of the existence of the funding arrangement might signal the strength of the case to the opposing party and encourage a settlement. On the other hand, in some common law jurisdictions where discovery may be more readily available, it may subject a claimant to a costly and time-consuming fishing expedition by the respondent. Needless to say, a balance has to be achieved between the mitigation of any conflicts of interest and the preservation of a party’s privileged and protected information.

7. Conflicts of Interest

The third-party funding market necessarily has to grapple with the issue of conflicts of interest (whether actual, potential or perceived) which arise as a result of the funder’s participation in a particular case. The issue of arbitrator conflicts of interest is addressed more fully in subsequent chapters.

A related issue is that of how the claimant’s legal team can mitigate or manage potential conflicts of interest arising between its duties to the claimant and its relationship with the funder. While the majority of funded cases proceed smoothly with an aligned interest between the funder and claimant (and legal team), there is always the potential for issues to arise. For example, a funding structure where the funder is entitled to a multiple of the capital invested as a priority over the claimant, means that there is a theoretical case outcome where the funder receives a healthy return (of say repayment of its investment plus a return of 3x the invested capital), but the claimant receives nothing. Such a structure (while not uncommon) can clearly give rise to tensions when it comes to considering an offer of settlement pitched by the respondent somewhere in around that level. Similarly, issues such as budget overrun, a change in legal representation during the proceedings, or a deterioration in the merits of the case can create situations where the interests of the claimant diverge from those of the funder.

The most common structure of a third-party funding arrangement is one which allows the law firm to maintain a fairly clear demarcation between the duties owed to the claimant and those (if any) owed to the funder. The claimant and the funder enter into an arrangement under which

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the funder provides the claimant with capital in order to finance the legal fees and costs associated with the arbitration. Under this structure, the claimant’s lawyer advises and owes duties only to the claimant (the funder typically having taken separate advice from its own external counsel).

However in reality, the relationships between funders and law firms often go much deeper. It may be for example that the client entered into the funding arrangement as a result of the law firm’s introduction or relationship. It may even be that the law firm relies upon the funder for financing across a portfolio of matters, which can make it more difficult to avoid or manage perceived conflicts of interest where a disagreement arises between the funder and one of the funded clients in the portfolio.

Some law firms utilize or recommend the services of independent brokers in order to maintain distance from the funder selection process and mitigate any perceived conflict issues.

ii. The Process

1. The Approach

The dispute funding market is changing rapidly, with a continued influx of new capital providers, greater competition amongst funders, and the increasing availability of alternative insurance-based structures. Since most clients are not repeat users of dispute funding, they often rely upon a specialist broker or lawyer with expertise in this area for advice and guidance and to manage the process throughout.

Regardless of whether or not a broker is used, any party considering third-party funding for a claim will be well-advised to simultaneously approach multiple prospective funders. This increases the chances of securing funding (as noted above, individual funds reject the vast majority of opportunities presented to them), while creating a competitive process to enable the terms of any funding offer received to be weighed up in the context of any competing offers available.

Once a decision has been made to approach prospective funds with a particular matter, careful funder selection based upon the case profile and specifics (taking into account each funder’s investment criteria), as well as the types of structure and commercial terms sought, will have a significant bearing on the eventual outcome.

Case presentation is also important. As noted above, funders’ investment decisions will be based upon a range of factors and a well-prepared and comprehensive case presentation will enable prospective funders to form a preliminary view on the case and move quickly to a decision on whether or not to offer terms.
2. **Case Assessment**

Each funder’s approach and decision-making process is different, as is the speed with which each can move from initial case presentation to execution of a funding agreement. The most common approach is a two-stage process. The first stage involves an initial (usually internal) evaluation of the opportunity by the funder. This will encompass the items discussed above, such as the case merits, amount of the funding request, claim value, legal landscape, enforcement, etc.\(^{39}\) If satisfied that the case meets the funder’s investment criteria, the funder will make an offer (usually in the form of a term sheet or conditional funding agreement). The offer will usually be subject to the funder completing a second more detailed due diligence process, often using external counsel. Given the time and expense incurred during the second phase, many funders request a period of exclusivity in order to complete this.

The requirement for exclusivity is not universal, but it is a relatively common practice amongst funders. While it should generally be accepted as a legitimate requirement by a funder about to embark upon an intensive and potentially costly due diligence process, it should also be approached with caution by claimants. Agreeing to a lengthy exclusivity period in a time-sensitive case can be highly damaging if the funding agreement is not executed at the end of the process.

Some funders also employ a third level of review, which requires submission of the claim and the proposed funding terms to an investment committee for a final decision.

3. **The Litigation Funding Agreement**\(^{40}\)

The Litigation Funding Agreement (“LFA”) sets forth the terms upon which the funding is provided to the claimant, including the extent of funding commitment, return structure, rights and obligations of the parties and termination rights.

For purposes of providing an overview, the sample Therium LFA contained within Nick Rowles-Davies’ book is useful, as is his explanation and those of other authors.\(^{41}\) However, each funder’s standard LFA is different and most LFAs eventually executed by a claimant are individually negotiated and therefore depart from the funder’s standard form to some extent. As

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\(^{39}\) See Mick Smith, in Shannon and Nieuwveld, Third-Party Funding in International Arbitration, pp. 28-33, for a discussion of the valuation of a claim from a funder’s perspective, including an overview of a matrix approach employed by Calunius Capital.

\(^{40}\) For a more thorough discussion, please see Goeler, *supra* at 2, pp. 11-72; Smith, *supra* at 20, pp.19-38; and Rowles-Davies, *supra* at 9, pp. 120-125, 221-247 (Appendix 1, which provides a copy of a sample Therium Litigation Funding Agreement).

\(^{41}\) See Goeler, *supra* at 2, pp. 11-72; Smith, *supra* at 23, pp.19-38; and Rowles-Davies, *supra* at 9, pp. 120-125, 221-247 (Appendix 1, which provides a copy of a sample Therium Litigation Funding Agreement). See also Maya Steinitz, *A Model Litigation Funding Contract*, 99 Iowa Law Review 711 (2014).
such, it is beyond the scope of this chapter to attempt to comment in detail upon the commonalities and differences between various agreements.

However, there are some provisions which are worthy of particular consideration. For example, the circumstances in which the funder may suspend or terminate the funding or potentially seek recourse against the claimant for the amount invested are especially important. The Association of Litigation Funders of England & Wales (“ALF”) Code of Conduct envisages the following grounds for the funder seeking termination of the LFA (the last of which potentially entitling the funder to recourse for the capital invested to that point):

“11.2.1 reasonably ceases to be satisfied about the merits of the dispute;
11.2.2 reasonably believes that the dispute is no longer commercially viable; or
11.2.3 reasonably believes that there has been a material breach of the LFA by the Funded Party.”

While on the face of it, these are reasonable grounds for the withdrawal of funding, the manner in which the merits and commercial viability of the claim are to be judged and by whom are significant.

The ALF Code of Conduct requires that any dispute about settlement or termination should be resolved by independent counsel. A dispute resolution clause along these lines is a common feature in many LFAs (including produced by funders who are not members of the ALF) to enable a funder to exercise reasonable termination rights, while protecting the client from a unilateral and unreasonable decision by the funder to cease funding.

It should also be noted that in addition to the LFA, various ancillary agreements may also be entered into as a part of formalizing the overall funding arrangement, such as the Priorities Agreement or waterfall agreement, Retention/Engagement Agreement with the Law Firm, and/or Insurance Policies. As noted above, the Waterfall Agreement is a particularly important document (or section within the LFA) and sometimes one of the more challenging items to negotiate, given that multiple parties, potentially with competing interests, need to agree to the framework.

II. Other Dispute Funding Models

Although third-party funding or dispute funding has only relatively recently emerged as a distinct industry, it should be viewed in context as one of a number of the alternative ways of financing arbitrations. This Section provides some examples of the other models that exist.

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43 See Goeler, supra at 2, p.33 (The priorities “agreement involves all relevant stakeholders in the claim and stipulates who will receive what in case of successful recovery.”); Smith, supra at 20, pp. 23-24 (describing and providing an example of a typical priority of payments structure).
A. Insurance

Insurance is one of the oldest alternative sources of funding for disputes. Liability insurance generally involves funding the "legal representation in any action to defend against liability or recover damages, or to pay any award, order, or judgment against the insured, or both." There are also specialized forms of legal expenses insurance, sometimes referred to as "before-the-event" (BTE) and "after-the-event" (ATE) insurance. Both forms of insurance are specifically intended to cover the insured’s liability for legal fees and costs incurred in relation to litigation or arbitration. Depending on the structure, coverage may be provided for the insured’s own legal fees and costs and/or the insured’s potential liability for the opponent’s legal fees and costs if the claim is unsuccessful.

BTE is taken out to cover the risk of possible future litigation arising. It is sometimes sold as an add-on to other kinds of insurance and is usually limited in the types of dispute covered and the level of coverage provided. It will provide funding for bringing a claim falling with the scope of cover, paying lawyers’, arbitrators’ and experts’ fees during the course of the arbitration. It may also cover an insured’s liability for a costs award in its opponent’s favour. A BTE insurer is remunerated through premiums paid in advance (usually annually). It has no interest in the proceeds of an arbitration which it supports, other than potentially for reimbursement of the amount funded. For that reason, being keen to minimize its expenditure, it will control the conduct of the claim as closely as it can.

ATE insurance (increasingly known as litigation/arbitration insurance) is taken out after a legal dispute has arisen and covers the risk that the insured party will be unsuccessful in the litigation/arbitration. The industry flourished in the UK in the early 2000’s and was historically aimed primarily at insuring the fee shifting (adverse costs) risk, as well as the claimant’s own ‘disbursements’, such as expert fees, barrister fees, court fees etc, on the basis that the law firm would be engaged on a conditional fee basis.

Today, the litigation/arbitration insurance industry is mature and well-established, albeit niche and highly specialized. Coverage may be provided for the insured’s attorney’s fees and out of pocket costs as an alternative or complimentary option to third-party funding. In addition, in forums and jurisdictions where fee shifting applies, insurance generally remains the most cost-effective way for parties to hedge the adverse costs risk. The UK is still one of the largest markets, but the industry is growing in the across Europe, North America and Asia and many insurers are

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44 James Clanchy, “Navigating the Waters of Third Party Funding in Arbitration” 82 Arbitration 222.
45 NIEUWVELD & SHANNON, at p. 6.
experienced in underwriting large, complex international arbitration (both commercial and investor/state).

Litigation/arbitration (ATE) insurance premiums can be structured in a number of ways, but a common model, which is unique to this type of insurance, is a “contingent premium” model, meaning that the insured only pays the insurer a premium if and when they are successful in the claim (in which case the premium is usually paid out of the settlement or damages award obtained, in a similar manner to a third-party funder’s return, although usually much lower in amount).

As the litigation/arbitration insurance market expands internationally, it is increasingly competing directly with (as well as in some instances supporting) the third-party funding market. In practical terms, a claimant considering third-party funding as an option may also and in parallel consider using insurance to cover it’s legal fees and/or out of pocket costs (both historic and future) in exchange for which it will only pay the insurer a premium if it wins the case and collects damages or a monetary settlement. In this form, litigation / arbitration insurance is structurally very similar to third-party funding. The only material differences are that the insurer does not provide day to day financing, but instead will pay out on an indemnity basis if the case is unsuccessful and that the insurance premium is typically much lower than the typical return sought by a third-party funder.

B. Loans, Corporate Financing, Equity-based and Inter-Corporate Funding

Arbitrations may also be funded through traditional loans, corporate finance, equity-based investments, or some hybrid. For example, a parent company may make a loan to a subsidiary to enable it to pursue a claim, or the shareholders, creditors or beneficial owners of an entity may provide financial support for the pursuit of a claim which will in turn provide a financial benefit which will flow back to them. Some types of funding are effectively a form of private equity.47

There have been some examples of third-party funders taking an equity position in the claimant entity and, as such, gaining control over its investment through traditional corporate governance (i.e., membership on the Board of Directors).

Corporate financing specifically to fund a party’s costs in a dispute can raise some of the same issues as third-party funding. Those issues, however, are usually resolved through traditional corporate governance mechanisms and existing rules that govern corporate relationships. For example, the potential for conflicts of interest between an arbitrator and a party extends not only to the party itself, but also to affiliates of that company.48

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47 Examples include in Churchill Mining PLC and Planet Mining Pty Ltd v. Republic Indonesia, ICSID Case No. ARB/12/14 and 12/40 (not public), and Crystallex International Corporation v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/11/2.

48 See IBA Guidelines on Conflicts of Interest.
C. Attorneys as Funders

Attorneys may effectively act as funders when engaged to act on a full or partial contingency fee basis. In either instance, the attorney bears some or all of the cost of the arbitration and assumes the risk of loss. A common structure involves the client financing the out of pocket costs and expenses (either from its own resources or with external financing) with the law firm forgoing payment of some or all its fees in exchange for a share of any award or settlement obtained. However, in some instances, the law firm may also agree to cover the out of pocket expenses, including tribunal fees, in exchange for a larger contingency fee.

This type of arrangement (especially where the law firm pays the out of pocket costs) is conceptually and structurally similar to third-party funding in many ways. It may also produce comparable economics from the claim holder’s perspective – the law firm’s share of the proceeds for taking a case on full contingency, including covering the out of pocket costs, may reasonably be expected to be similar to the share required by a funder for financing the case in full. Where, as is not uncommon, the law firm and a third-party funder share in the risk/reward (e.g. by the firm forgoing payment of fees with the funder covering the expenses), each party should expect a share of the proceeds which is commensurate with the relative risk taken by each.

Although there are a number of law firms that have amassed significant “war chests” to support contingent fee work, many of the more conservative law firms are not able to assume significant fee risks on large claims. Such firms have historically been more likely to turn to third-party funders. However, developments in the availability of insurance options to enable law firms to hedge fee risk, as well as the rise in law firm portfolio financing is enabling historically conservative firms to take on more contingent fee work, while mitigating fee risk and cash flow concerns.

In addition to traditional contingency fee arrangements, other alternative fee arrangements may divide the risk between clients and attorneys. Examples include a reduced hourly rate, or capped fees, but with a “success fee” added as a bonus if the claimant wins, as well as fee collars, staged fee caps, etc. Such arrangements will often bear much less resemblance to third-party funding and may in practice represent only a small departure, in risk/reward terms, from the law firm’s normal hourly rate model. However, such a fee agreement is still highly relevant to the third-party funding structure. For example, a fee cap which ensures that there is no risk of budget overrun will be a positive feature from the perspective of potential funders and may in some instances be preferable to a discounted hourly rate.

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49 See SAHANI, at pp. 5, 8.
50 ‘Game-changer’ for UK litigators with launch of first DBA insurance, Solicitors Journal, 24 May 2017
With pro bono lawyering, the attorney may absorb all or most of the cost of representing a client, who is usually indigent or otherwise unable to pay, without any guarantee or reasonable expectation of reimbursement or profit. To date, pro bono representation is relatively rare in international arbitration, but certain NGOs are active as *amici* and it is plausible they could end up providing representation for certain claims that implicate causes they support. Although it has some similar markers and may raise some similar issues, pro bono representation is not usually treated as a type of “financing” because no money changes hands. But as Sahani and Niewold point out, “the practical effect of the attorney representing the client without requiring payment could certainly be viewed as a form of ‘financing’, because the financial burden of legal representation has been shifted from the client to the attorney.”

III. Current Trends and Evolution of Funding Models

The rising global prominence of dispute funding has led to some jurisdictional liberalization and a re-analysis of the status of champerty and maintenance in a number of jurisdictions, with some notable exceptions, such as Ireland, where the Supreme Court recently held that third-party funding was unlawful on the ground of champerty.

In its modern incarnation, dispute funding has the ability to transform a legal claim into a financial asset, which can potentially be monetized or used as collateral in order to secure finance. At present, dispute funding is moving more into the realm of corporate finance, with increasingly diverse and sophisticated options becoming available.

At the same time, the global third-party funding market is growing exponentially, both in terms of the number of funds operating, and in terms of the amount of capital available. However, when it comes to individual dispute funding, many funders have similar appetites and underwriting criteria, meaning that in some jurisdictions, the market is become increasingly crowded, forcing funders to compete more aggressively for opportunities and explore alternative ways of deploying capital. What follows are some examples of the ways in which the market is evolving.

A. Portfolio funding

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51 SAHANI, *supra* at 7, p. 6.

52 For example, *Arkin v Borchard Lines Ltd and others* [2005] EWCA Civ 655; See also Hong Kong’s Legislative Council’s 2017 amendments to the Arbitration Ordinance (Cap. 609), Part 10A (ss.98E – 98W) abolishing the doctrines of champerty and maintenance for arbitration.

53 Persona Digital Telephony Ltd & ors v The Minister for Public Enterprise & ors [2017] IESC 27
Portfolio funding is gaining prominence as an alternative to financing on a case-by-case basis and is an approach that many funders now actively promote. A portfolio arrangement can be structured in many ways, but there are two major types of arrangements: (1) finance structured around a law firm, or department within a law firm, where the claim holders may be various clients of the firm; or (2) finance structured around a corporate claim holder or other entity, which is likely to be involved in multiple legal disputes over a relatively short period of time.

Structuring finance around multiple claims under either model usually involves some form of cross-collateralization, meaning that the funder’s return is dependent upon the overall net financial performance of the portfolio as opposed to the outcome of each particular claim. This type of structure may enable the entity (e.g., the law firm or corporate client) to secure third-party funding more quickly, on pre-arranged terms, and, depending on the structure, the ability to benefit from the overall success of the portfolio. Additionally, there may also be economic benefits to this approach – if the funder’s risk is spread across multiple claims, this should in turn dictate a lower cost of capital for the funded party (although this does not always materialize in practice).

From a corporate claim holder’s perspective, portfolio financing offer some interesting options, such as the possible inclusion of some types of cases within the portfolio that would not ordinarily be capable of being funded on an individual basis (e.g., defence or non-monetary cases). This is possible because the funder’s return is collateralized by the claimant cases within the portfolio. Such a model may also enable the corporate claimant to monetize the portfolio, drawing capital secured against the dispute portfolio to utilize not just for financing legal expenditure but for other business purposes and/or to declare as profits.

A law firm portfolio may be structurally similar, where the finance is provided to support a law firm’s contingency fee portfolio, with the funder’s return pegged to the law firm’s success. Again, such a model potentially allows for the law firm to draw capital more flexibly than a single case funding scenario, as well as enabling, for example, fee overruns on one case to be offset by another case that is operating below budget. Under the above model, the funder may have no direct contractual relationship with the law firm’s clients, as the portfolio funding agreement is only between the law firm and the funder.

An alternative variety of law firm portfolio (which may exist alongside the structure described above) is one where the law firm’s clients enter into individual funding agreements with the funder, but the terms of those agreements and/or the process for putting finance in place is dictated by the law firm’s wider arrangement with the funder. Such arrangements are arguably not portfolio arrangements as defined above, as it is unlikely that cross-collateralization would be possible amongst the funded cases. (It would be surprising for one claimant to agree that some portion of its claim proceeds should go to offset losses suffered by another unrelated client of the firm.) Such arrangements can still offer clear benefits to the law firm, if for example the funder offers an expedited due diligence process, pre-agreed funding terms, etc. However, such

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54 Reference the well-publicized arrangement involving British Telecom and Burford Capital is a good example of the practice.
arrangements do create potential conflict of interest issues, which law firms need to navigate carefully.

B. Going Beyond Financing Legal Cost

Another developing area with respect to the litigation finance market is the increasing willingness of funders to consider (and in some instances, actively pursue) opportunities where the funder’s capital is to be used for a purpose other than solely financing legal fees and costs. For instance, funders are providing working capital to the claimant entity during the life of the proceedings, providing financing to enable the claimant to discharge pre-existing liabilities or simply providing an advance on the damages to the claimant. Such structures are substantially similar to “traditional” third-party funding, in that the funder commits to provide a certain amount of capital with the funder’s return tied to the success of litigation or arbitration. Using this model, a claim holder can use the claim as an asset in order to raise capital for a variety of potential purposes.

In the early life of the market, this structure was viewed by many funders as unattractive. Where offered, it was usually only relatively modest in sum and incidental to a larger funding provision for legal costs. However, as the market has become more competitive, funders are increasingly seeking to differentiate themselves and offer alternative applications for their capital, including in some instances inviting prospective clients to consider third-party funding not only as a means of financing their litigation but simply as a way of raising capital on a non-recourse or limited recourse basis.

That said, the practical availability of such arrangements should not be overstated. Whether a deal is capable of being structured in practice depends upon a large number of factors. The dynamics of such arrangements may be unattractive. For example, if the majority or entirety of the funder’s committed capital is to be drawn on day one, this may be a significant departure from the traditional litigation finance economics, where the funder expects its funding commitment to be gradually drawn down during the life of the proceedings. This may entail a greater cost of capital to the funder and therefore less favourable funding terms.

Additionally, there is the problem of the case, itself. If the claim holder wishes to use the claim to raise capital, it is likely that they may also require financing for legal costs. In such a case, the overall funding commitment will be materially larger than it would have been if the funding was limited to solely to the arbitration budget, therefore requiring a much larger claim value in order for the arrangement to work. Funders will be wary of a deal that puts too much cash into the client’s pocket upfront or too heavily erodes the client’s expected net recovery, because of the risk that the client may lose interest in the outcome of the case and not commit itself fully to maximizing the chances of success.
C. Equity Financing

As noted above, under the traditional model of dispute funding, the funding commitment, the expected level of return, and the terms of the investment are set out within and governed by contract (e.g., the litigation funding agreement (“LFA”) and/or the Priority Agreement setting out the waterfall of distribution). However, if the claim holder is a special purpose vehicle (“SPV”) or entity with no other material assets other than the claim in question, the third-party funder may be able to structure its investment and return by purchasing equity in the claimant entity. Under this model, the funder’s return is derived from distributable profits generated from the success of the arbitration, as opposed to a contractual return. Such a structure may offer a number of potential benefits. It may, for example, enable the funder to take greater or total control over the litigation without running afoul of champerty restrictions. For example, it has been expressly recognized by the Irish Supreme Court that structuring investment in this way would not be deemed to be champertous, whereas third-party funding would be.55

Furthermore, owning a stake in the claim holder may enable the funder to be brought within the circle of privilege, allowing the funder access to all privileged information without concerns about a potential discovery application for information shared with the funder.

D. Assignment/Sale of Claims

There are many situations where the outright sale of the claim may be preferable for both the claim holder and the funder to the ‘traditional’ third-party funding model. A claim holder may view lengthy litigation or arbitration proceedings as a costly and time-consuming nuisance and would happily transfer the rights to another party in exchange for an immediate payment of cents on the dollar. From the funder’s perspective, having total, unfettered control of the claim (including, in particular, control of settlement decisions) may be highly desirable.

In common law jurisdictions, the outright sale or assignment of claims may not be permitted and in jurisdictions where champerty exists, funders may be prohibited from taking control of another party’s litigation in this way. The traditional definition of third-party funding in common law jurisdictions will therefore typically describe the arrangement as an investment in the claim holder’s litigation in exchange for a financial interest in the outcome,56 as opposed to an outright sale.

56 See ALF Code of Conduct, supra at 26.
However, as noted above, in some civil law jurisdictions, funders may adopt a model where the claim is simply purchased outright and pursued by the purchaser, possibly aggregated to other similar claims in order to produce costs savings. The market for the purchase and aggregation of cartel damages claims in Germany and the Netherlands is a good example of this approach, although there are few examples of international arbitration claims being arrogated in this way.

In the UK, the exemption for liquidators which allows the assignment of claims to other parties has led to a rise in the practice of funders offering not to fund, but rather to buy claims arising in insolvency. The structure may involve an upfront purchase price (allowing an immediate distribution to creditors), a deferred structure where the funder pays a share of any amounts recovered to the insolvent estate, or a combined part upfront, part deferred payment structure.

E. Enforcement Financing

By definition, the non-recourse litigation financing model requires the funder to accept both what may be described as “litigation risk” (i.e., the risk of an adverse ruling or award) and enforcement or collection risk. In other words, in order to see a return on invested capital, the funded party must not only win the case, but must also successfully enforce the award.

Traditionally, many third-party funders have been more comfortable assessing litigation risk than enforcement risk, which is perhaps a reflection of the fact that most third-party funders are managed by former lawyers. In the early stages of the market’s development, it was common for funders to simply turn down cases where enforcement was likely to be challenging due to the lack of visibility over or location of assets. However, as the market has developed, funders have recognized that many of the largest and potentially most lucrative disputes might require an acceptance of material enforcement risk. Today, many funders have in-house asset-tracing and enforcement capability and may seek to differentiate themselves on that basis. Similarly, there are a number of funders that originally started out as award enforcement or debt recovery agencies, but have gradually embraced opportunities to get involved and finance contested claims at earlier stages in the arbitration process and now finance contested claims. Some such funders may now be known generally as third-party funders, even though their businesses may pre-date the modern third-party funding industry. Other may not describe themselves as third-party funders, but nevertheless offer similar structures.

In practice, enforcement financing may be expressly or implicitly built into an agreement to fund an arbitration claim on the basis that the funder will not see a return until the award is successfully enforced. Funders will also often consider enforcement-only opportunities, where an award has already been obtained and the claimant seeks financial support and/or expertise to secure collection. Enforcement financing is therefore a necessary component of third-party funding and something which most funders today provide, albeit with different risk appetites and levels of expertise.
F. Assignment / Sale of Awards

Related to the purchase of claims (see discussion infra) is the market for the purchase / assignment of awards and judgments. This practice is permitted in most jurisdictions and pre-dates modern concepts of third-party funding. Many of the funds that operate in this space would not consider themselves to be third-party funders, however many third-party funders will also consider such opportunities. Like claims sales, the sale of awards can be structured in a number of different ways, from a simple upfront purchase price to a payment which is in whole or in part based upon the amount collected.

IV. Conclusion

In the last decade, the global litigation finance industry has grown beyond all recognition and continues to expand, both in terms of the number of funders operating and in terms of the amount of capital raised and deployed. This market growth has gone hand-in-hand with rising awareness amongst the legal community. There are few arbitration attorneys that are not at least aware of the basic premise of third-party funding and there is an ever-growing proportion that have first-hand experience of the market.

Much of the focus of the larger litigation funds today is on encouraging greater corporate use of litigation finance. While third-party funding was considered an option of last resort for financially distressed claimants, funders are increasingly encouraging corporates with strong balance sheets to use litigation finance as an alternative to tying up their own capital in litigation or arbitration. The idea and advantages of off-balance sheet litigation and turning in-house legal departments into profit centres are well-established.

While the market is becoming more diverse, the larger funders have tended to follow a relatively similar pattern. They commonly seek primarily to invest in a relatively small volume of very large commercial disputes and portfolio’. The amount of capital committed to each investment tends to be in the millions of dollars, the claim values in the tens, hundreds of millions or more and the funders are expecting to make a multiple return on the capital invested in successful cases. Investing in this profile of cases with the levels of financial risk involved tends to necessitate both high rejection rates and detailed due diligence. While many funders advertise speed of execution by comparison to their competitors, the reality is securing funding can be a lengthy and complex process. More streamlined options for financing smaller to medium-sized claims are still limited in many jurisdictions, although this is an area which is gradually attracting interest from the litigation finance market and is expected to continue to develop in the next few years.
The growing number of funders has already produced and should continue to yield positive developments for prospective users of dispute funding, requiring funders to compete on speed and cost of capital in order to win business and meet target capital deployment levels.

Third-party funding must also be seen in the context of the wider arbitration finance and risk management market. As noted above, law firms may play an increasingly prominent role in this regard. Currently, some historically conservative firms are using external finance and insurance to support developing contingency fee portfolios. As more innovative financing solutions become available to law firms, potentially with lower capital costs than traditional third-party funding, it is possible that we may see law firms and funders start to compete for opportunities.

In addition, the dispute risk insurance market is developing rapidly, growing in prominence and expanding into new markets and jurisdictions. These insurance options are now being presented by lawyers and brokers alongside third-party funding as part of a broader discussion about the potential options available to finance or de-risk arbitration.
Chapter 3
Definitions†

I. Introduction

In their consideration of various substantive topics, Task Force discussions frequently returned to important and fundamental questions about the definition of third-party funding. This focus on definitions is not surprising given the need for a clear understanding of the object and the scope of the Task Force’s work and, relatedly, of any recommendations or guidance produced by the Task Force.

For these reasons, and in light of the range of definitions adopted by various entities seeking to regulate third-party funding, it was decided that the Task Force Report would benefit from a deliberative analysis of issues implicated in delineating meaningful definitions of third-party funding. This Chapter provides that analysis, including a survey of various definitions adopted in other sources, and a conceptual analysis of functional aspects of funding that may affect definitions. This Chapter is intended to be read as background to other Chapters, each of which effectively adopts a specific definition of the funding activities addressed in its analysis.

This Chapter proceeds in the following parts: Part 1 provides general background about consequences and concepts implicated in different definitions. Part 2 provides a brief definitional overview of the full range of means for funding disputes that are within the scope of the broad Working Definition that is the starting point for the Task Force. Part 3 provides a survey of the definitions that have been adopted by various institutions, legislation, treaties, policy makers, and scholars in the international arbitration context. Part 4 engages in a functional analysis of certain key features of third-party funding and briefly examines the extent to which such features raise issues that are distinct to third-party funding. Finally, Part 5 provides an overview of the more specific definitions adopted in various subsequent Chapters in order to limit the scope of their application to the specific topics taken up by those chapters.

II. Background

In recent years, courts, commentators, and policymakers have identified the rise of a new industry of non-parties that fund parties’ costs in various sectors of international arbitration. Despite their increasing presence in international arbitration, the precise definitions of “third-party funder” and “third-party funding” continue to be subject to considerable debate. Even funders

† Primary contributors to this Chapter include Catherine Rogers, Stavros Brekoulakis, James Clanchy, and Duarte Henriques. Mr. Ahmed El Far also contributed valuable research assistance.
themselves disagree over the precise definition of third-party funding or whether it is even capable of definition. Several reasons explain this definitional difficulty.

One reason for definitional ambiguities is that modern outside funding of a party’s costs can resemble, or be co-terminous with, other forms of financing that have existed long before the current phenomenon. For example, in some jurisdictions, contingency fee arrangements are widely used to provide legal representation and in some instances cover claimants’ expenses. Although rarely explicitly referenced as a form of third-party funding, the practice is inevitably subsumed in many general definitions that refer to a non-party funding for a case, unless expressly excluded. Even if a law firm does not advance any specific amounts for costs, they are effectively contributing something of material value—legal services—in exchange for an interest in the final award.

In maritime arbitration before-the-event (BTE) insurance has funded many claims since the Nineteenth Century, and continues to play an important role both in and apart from maritime-related disputes. Others argue that modern funding arrangements are largely indistinguishable from after-the-event (ATE) or traditional liability insurance, and from conventional forms of corporate financing through which a shareholder or related corporate entity may indirectly finance a party’s costs in an international arbitration.

Defining “third-party funding” is also difficult because a wide range of funding models exists, and that range is rapidly evolving, even since when the Task Force was constituted. For example, funding may be structured as debt instruments, equity instruments, risk-avoidance instruments, or as full transfers of the underlying claims. More recently, some funders have taken an equity position in a company or are engaged in “portfolio financing” of an identified range of

57 See Maxi SCHERER, Aren GOLDSMITH and Camille FLÉCHET, “Third-Party Funding in International Arbitration in Europe: Part 1 – Funders” Perspectives, 2 RDAI/IBLJ (2012), p. 209-10, available at: <https://www.transnational-dispute-management.com/news/20120312.pdf> (last accessed 27 October 2016), reporting on a roundtable, attended by various major litigation funding firms, where the participants could not agree on a definition of third-party funding. This confusion is apparent even at a terminological level. As one commentator describes, “[t]he nomenclature to describe this kind of third-party capital investment in arbitration or litigation claims is all over the map and woefully undescriptive. It has been referred to as “third-party funding”, “third-party litigation funding or financing”, or most commonly “alternative litigation funding or financing”’. Michele DESTEFANO, “Non-Lawyers Influencing Lawyers: Too Many Cooks in the Kitchen or Stone Soup”, 80 Fordham L. Rev. (2012) p. 2791 at p. 2794.

58 For example, new Hong Kong legislation expressly permits third-party funding, but expressly acknowledges that contingency fee arrangements are still prohibited. This exclusion suggests that, in the absence of such an exclusion, its definition of third-party funding could include lawyer funding through contingency fees.


60 Anthony J. SEBOK, “The Inauthentic Claim”, 64 Vand. L. Rev. (2011) p. 61, at p. 63-67. Given the potential overlap between modern non-recourse third-party funding and other traditional means of supporting litigation expenses, some on the Task Force argued that the Report should adopt the term “modern third-party funding” to distinguish more recent phenomena from more traditional forms of litigation support. For reasons explained in greater detail in this Chapter, however, the Task Force decided not to circumscribe its analysis to modern forms, but instead sought to locate more modern forms of funding in the constellation of existing forms.
cases involving a particular party or law firm. In the latter instance, funding is provided to the law firm, not the party, which can raise additional practical and definitional challenges.

Meanwhile, third-party funders may become involved either before a claim is filed or later in the process.61 Some funders specialize only in award execution or funding for expert witness costs, while others fund all costs, including a potential adverse award of costs. Funders also separately incorporate “special purpose vehicles” to facilitate the funding arrangement.62 In addition to the variety in funding models, modern funding is expanding as a result of an influx of new funders and the expansion of funding into new regions and jurisdictions.63 Newer funding models increasingly also combine with equity positions, long-term relationships with parties and law firms, and various types of insurance.

The proliferation of funding models raises questions about how to define funding for the purpose of the Task Force’s study and any potential recommendations. Disagreement existed on the Task Force about whether to focus its study on the narrow, modern practice of case-specific non-recourse funding, or to adopt a broader definition that takes account not only modern non-recourse models, but other forms of financing that are conceptually or functionally similar and/or function as alternatives in the same market. As explained in greater detail below, for the purpose of study and discussion the Task Force adopted a broad definition. Meanwhile, specific recommendations in this Report are based on more targeted, narrowly tailored definitions.

Given the pace of developments in the field, this Chapter includes not only a discussion of conceptual definitions of funding, but also an analysis of the functional similarities and differences among different types of financing that may either come within a definition of funding or be considered by analogy alongside funding. Like debates about the scope of our working definitions, at least one member on the Task Force questioned the utility of including any discussion of functional aspects of third-party funding.64 Given that various national, international, and scholarly debates about funding often include analogical reasoning based on functional distinctions

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62 See Cento VELJANOVSKI, “Third-Party Litigation Funding in Europe”, 8 J.L. Econ.& Pol’y (2011) p. 405 at p. 430 (‘[Third-party litigation funding investors] rely on Special Purpose Vehicles, which . . . are legal entities created for . . . the acquisition, financing, or both, of a project or the setup of an investment. They are usually used because they are free from pre-existing obligations and debts, and are separate from the parties that set them up for tax and insolvency purposes.’).

63 For example, third-party funding only become permissible in Hong Kong and Singapore in 2016-17 as a result of legislative changes in those jurisdictions that eliminated the doctrines of champerty and maintenance for international arbitration. Meanwhile, litigation finance has also recently arrived in Latin American with the emergence of Leste based in Brazil and Lex Finance based in Peru.

64 The Task Force benefitted from the expertise of its Members and consultation with other experts on various forms of litigation support, including ATE, BTE, and liability insurance. During the public comment period, it will also co-host, together with The Law Society of England and Wales, a roundtable discussion to engage directly with members from the London insurance and maritime markets. One Member of the Task Force considered these sources and efforts inadequate for the Task Force to address issues relating to insurance.
between modern funding and other sources of litigation finance, functional aspects of third-party funding are included in this Chapter as a useful point of reference.

One challenge in analysing functional aspects of third-party funding is that funding arrangements vary significantly among different funders and funding agreements. Some funding agreements permit or require active participation of the third-party funder in key strategic decisions in the arbitration. Other agreements provide for a more limited role for funders, providing only for periodic updates and limited opportunities for intervention. One fairly conventional model for modern funding agreements provides for funders to receive a percentage of recovery, with the percentage increasing over with the passage of time since the initial investment. While most funders invest for profit, not all do, particularly if they fund responding parties. For example, in the investment arbitration case brought by Philip Morris against Uruguay, The Bloomberg Foundation and its ‘Campaign for Tobacco-Free Kids’ provided outside financial support for the Uruguayan government. While this arrangement involves funding of a case by a third party, funding was for a respondent (not claimant) and the funder’s interest was not financial, but instead was tied to the political and policy implications of the award. Respondent States could also, as occurs in WTO proceedings, be funded by another State or, as has been reported by some funders, be funded through a model similar to after-the-event insurance.

III. The Task Force Working Definition

Given the range of possibilities, and the likelihood that additional variations will develop and flourish, this Report has taken as a starting point a broad Working Definition of third-party funding. While each subsequent Chapter contains its own definition applicable to the issues it

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66 See Lisa Bench NIEUWVELD and Victoria SHANNON, Third-Party Funding in International Arbitration, (Kluwer 2012) p. 2. For the purposes of this Report, “international arbitration” refers to both commercial and investment arbitration, but generally excludes maritime arbitration. In all respects that are relevant to this Report, maritime arbitration is a distinct field to which analysis and recommendations of the Task Force should not be applied. For example, maritime arbitration has distinctive internal rules, specialized arbitral institutions, a specialized body of practitioners, and a well-established history of funding maritime disputes. [SB: Given the importance of maritime arbitration and the well-established tradition of funding in this industry, I would consider moving this text here up in the main text above.

There was some disagreement on the Task Force about the viability of carving out maritime arbitration, given wide range of disputes that may fall in this category. Nevertheless, “maritime arbitration” is a term frequently used by practitioners and scholars to describe a broad range of arbitration disputes that arise out of circumstances between parties engaged in maritime affairs, and/or to arbitrations brought pursuant to maritime arbitration rules, such as those of the London Maritime Arbitration Association.

While this Report does not extend any of its recommendations to maritime arbitration, it includes references to funding arrangements that exist in the maritime field, for purposes of comparison only, because its long traditions are a helpful and important point of reference for analyzing modern funding arrangements.
addresses the Task Force’s work considered all types of funding that would fit within the following definition:

The term ‘third-party funder’ refers to any natural or legal person who is not a party to the dispute but who enters into an agreement either with a disputing party, an affiliate of that party, or a law firm representing that party:

a) in order to provide material support or to finance part or all of the cost of the proceedings, either individually or as part of a selected range of cases, and

b) such support or financing is provided either through a donation or grant or in return for remuneration or reimbursement wholly or partially dependent on the outcome of the dispute.

This broad definition facilitates consideration of the full range of funding models, as well as close analogies that provide important context.

The key elements of this definition are 1) an agreement; 2) with an entity that is not a party to the dispute; 3) the provision of financing or material support; and 4) either through a grant or in return for remuneration or reimbursement dependent on the outcome of the dispute. This Working Definition not only includes respondent-side funding, which some narrower definitions exclude, but also contingency fee funding by law firms, and certain types of insurance, to name a few examples. It applies not only to funding models that are premised on an expectation of a return on investment, but also to pro-bono representation and funding for non-profit purposes.

This definition is also intended to apply not only to individually funded cases, in which a funder’s support is directed specifically at individual cases, but also to newer models of funding. For example, this definition comprehends funding of a portfolio of claims held by business or represented by a law firm, or in financing provided to a law firm and collateralized by funds anticipated to be received from cases represented by that firm.

The purpose in adopting such a broad Working Definition is to ensure that the Task Force considers the full range of funding models and engages in careful analysis of the nature of the issues under consideration. Using a broad definition as an analytical starting point also facilitates examination of the extent to which issues under consideration are identical to, similar to, or different from those that arise or do not arise with respect to other more long-standing forms of funding.

For example, definitions that are too narrow may either exclude certain types of funding or preclude clear application of specific rules or guidelines that are intended to apply to third-party funders. For example, a special purpose vehicle created to fund one case might avoid easy application of the IBA Guidelines on Conflicts of Interest in International Arbitration (IBA...
Guidelines on Conflicts) that require disclosure and possible disqualification of an arbitrator who has been reappointed several times in a case involving the same funder. 67

In another example, many existing definitions that require financial interest in the award would exclude respondent- or defence-side funding (where no counter-claim has been filed). Respondent- or defence-side such funding undertaken, for example, to generate favourable precedent or advance policies implicated in the award, can raise concerns identical to those in modern claimant-side third-party funding. For example, an arbitrator may represent or sit on the Board of Directors of a non-governmental organization that is funding an arbitration or otherwise conflicted with a non-party that is providing funds for the dispute.68

Narrower definitions that do not consider functional similarities between modern third-party funding and other forms of dispute funding also may raise questions about coherence and fairness. For example, in some cases insurance companies or pro bono supporters may exert influence in selecting an arbitrator or making case management decisions that are functionally identical to modern third-party funders. If these sources of funding are definitionally excluded from consideration, resulting conclusions and recommendations for new regulation or guidance might draw lines that seem arbitrary. Conclusions and recommendations based on narrow definitions might also inadvertently preference one form of funding over another, even though they function as equivalents or alternatives, compete in the same market, or implicate identical issues.

Debate existed on the Task Force about whether this Working Definition would extend also to BTE insurance. The argument against inclusion is that premiums for BTE insurance are paid before any claim is initiated, and BTE insurer’s remuneration or reimbursement for its services is paid exclusively through these premiums and is not “dependent on the outcome of an arbitration.”

By contrast, others regarded BTE insurance 69 as coming within the Task Force’s Working Definition because a BTE insurer will be able to recover costs only in the event a claimant prevails, even if not by directly enforcing the costs award. In this way, the financial interests of a BTE insurer may be considered “dependent on the outcome of the dispute.”70 As described in Chapter


68 This situation arose in Quasar de Valores SICAV S.A. et al. v The Russian Federation, (SCC Arbitration No. 24/2007) Award (20 July 2012), para. 222. In that case, the funder, Group Menatep Limited, was a former majority shareholder in the Russian oil company Yukos (rather than a commercial third-party funding entity) and there was no formal written funding agreement that required claimant to reimburse Menatep. Speculation is that Menatep was funding the case in an effort to create a favorable “precedent” that would be helpful in its future, much larger, shareholder dispute against Russia under the Energy Charter Treaty. See Victoria SHANNON, “Revealing Not-for-Profit Third-Party Funders in Investment Arbitration”, available at <http://oxia.ouplaw.com/page/third-party-funders> (last accessed 19 August 2017).

69 For a description of BTE insurance, see Chapter 2, at p. 24.

70 There was further debate on the Task Force about whether BTE insurance would come under the IBA Guidelines’ definition. That issue is discussed below.
Two, like modern third-party funding, BTE insurance “will provide funding for bringing a claim falling within the scope of cover, paying lawyers’, arbitrators’ and experts’ fees during the course of the arbitration.”\(^71\) Unlike modern third-party funding, a BTE insurer “has no interest in the proceeds of an arbitration which it supports,” but because it can potentially be reimbursed as a result of the award, a BTE funder will, like a modern third-party funder, “control the conduct of the claim as closely as it can.”\(^72\)

Similarly, there was debate about whether ATE insurance\(^73\) would come within the Working Definition because ATE insurance does not involve financing. Like other types of third-party funding, however, premiums under most ATE policies are only payable in the event of success. As one scholar explains, “This means that the insured claimant … is only liable to pay the premium if the claim is won [and]…if the insured loses the case, no ATE premium is due.”\(^74\) Under such policies, because the ATE insurer will recover payment for policies only in the event of an award in favour of the insured, most on the Task Force regarded ATE insurance as being tied to the outcome of a dispute in a manner that brings it within the Working Definition. In addition, some ATE policies provide for reimbursement not only of an adverse cost award, but also for coverage of a party’s own legal fees and costs,\(^75\) which makes it direct competition for and more closely resemble modern forms of third-party funding such that separating it out from the definition was regarded as an artificial curtailment.

In addition, as discussed in greater detail below, in various respects, ATE, BTE, and liability insurance providers also functionally resemble third-party funders because their financing or support is predicated on a substantive assessment of claims to determine their likelihood of success. Insurers may also (depending on the policy and market) either select counsel or, in those jurisdictions where lawyers do not have a monopoly on legal services, BTE insurers may directly take on legal representation of the claim.\(^76\)

Narrower definitions that do not consider functional similarities between modern third-party funding and other forms of dispute funding may raise questions about coherence and fairness. Notably, prior to recent reforms introduced by the IBA, the ICC and SIAC, insurance was not

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\(^71\) See Chapter 2, at p. 24.

\(^72\) Ibid.

\(^73\) For a description of ATE insurance, see Chapter 2, p. 25.

\(^74\) Cento VELJANOVSKI, “Third-Party Litigation Funding in Europe”, 8 J.L. Econ.& Pol’y (2011) p. 405; see also Marco DE MORPURGO, A COMPARATIVE LEGAL AND ECONOMIC APPROACH TO THIRD-PARTY LITIGATION FUNDING, 19 Cardozo J. Int'l & Comp. L. 343, p. 353 (2011) (“From the viewpoint of third parties, ATE insurance is another way to invest in the outcome of litigation. ATE insurance is a particular type of insurance that can be taken out after an event, such as an accident that has caused an injury, to insure the policyholder for disbursements, as well as any costs should he lose his case.”). In addition, under some policies, premiums for the policy are only due dependent on particular outcomes, such as if the insured wins the case. See also overview of ATE and BTE insurance in Chapter 2, at pp. 24-25.


generally required to be disclosed in international arbitration. The revised IBA Guidelines, however, recognize that similar types of conflicts of interest may arise with respect to various types of insurance (for example, if an arbitrator sits on the board of directors of an insurance company, or owns substantial stock in it) in the same manner they arise with modern third-party funding. A narrow definition inadvertently preferences one form of financing over another, even though they function as alternatives, compete in the same market, and implicate identical issues.

Despite adopting this broad definition for the purposes of the Task Force’s analysis and discussions, later Chapters generally adopt narrower definitions so any recommendations or guidance is specifically targeted to particular issues. For example, insurance markets and the participation of insurers in adjudicatory proceedings are already generally regulated in various legal regimes through national procedural rules (in the litigation context) and professional ethical regulations. Prior to recent reforms introduced by the IBA, the ICC and SIAC, insurance was not regulated or required to be disclosed in international arbitration.

Meanwhile, in a similar vein, P&I and FD&D clubs have membership agreements and internal professional norms and traditions regarding representation of members, which appear to work well for their members. Finally, contingency fee arrangements are generally regulated through national attorney regulation, and potential conflicts with law firms providing contingency fee funding are governed by other sources aimed at the conduct of lawyers, such as the IBA Guidelines on Conflicts’ provisions regarding conflicts with attorneys and law firms, and the IBA Guidelines on Party Representatives in International Arbitration.

Given these definitional complexities, each topic considered in the subsequent Chapters required independent reconsideration of the broad Working Definition of third-party funding to determine the scope consideration, the nature of any potential recommendations, and the conduct and entities to which such recommendations might apply. This Chapter provides general background regarding definitional aspects of third-party funding that informed the Task Force’s discussions. It also attempts to locate more specific definitional decisions regarding recommendations in subsequent chapters within a broader analysis of the complexities involved in defining third-party funding.

77 [Insert references here to specific examples of regulation of insurance markets and of insurers, which relate to issues covered in other chapters of the report.]
79 See IBA Guidelines on Conflicts of Interest, 3.1.3.
80 Notably, Article 4 of the IBA Guidelines on Party Representatives requires “A Party should promptly inform the Arbitral Tribunal and the other Party or Parties of any change in such representation.” This provision, along with general procedures and practices that require disclosure of representation at the commencement of an arbitration, ensure that arbitrators are aware of the participation and identity of any attorneys or law firms in an arbitration.
IV. Survey of Existing Definitions

A. Legislation and Codes of Conduct

Debate exists in some domestic contexts about whether and to what extent third-party funding should be permitted or regulated. As a result, national laws regarding third-party funding in domestic litigation vary considerably.

To date, however, only two States appear to have taken any action to regulate, and therefore define, third-party funding in international arbitration. These legislative efforts have been undertaken as part of an effort to legalize the use of funding in international arbitration, which had previously been prohibited under the doctrines of champerty and maintenance.

Singapore has recently amended its law and permit modern third-party funding.81 For that reform, the definition of third-party funding is found in the recent Civil Law Amendment Bill and in the Civil Law Regulations.

The Civil Law (Amendment) Act 2017 defines third-party funding as “a person who carries on the business of funding all or part of the costs of dispute resolution proceedings to which the person is not a party.”82 A “third-party funding contract” is defined as:

“a contract or agreement by a party or potential party to dispute resolution proceedings with a Third-Party Funder for the funding of all or part of the costs of the proceedings in return for a share or other interest in the proceeds or potential proceeds of the proceedings to which the party or potential party may become entitled.”83

Under these provisions, the definition of a “third-party funder” appears to be considerably broader than the definition of a “third-party funding contract.” It is uncertain whether this distinction was intentional, and if so, what the intent was behind the drawing of this distinction. Notably, the definition of third-party funding contracts for the purposes of the Act does not appear to extend to non-commercial funders (such as individual persons), because they do not “carry on business” as a funder. Meanwhile, the provision that the funding contract provide for “a share or other interest in the proceeds or potential proceeds of the proceeding” would seem to preclude pro-bono or

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81 Civil Law (Amendment) Bill 2016 and Mediation Bill 2016 were introduced for First Reading in Parliament on 7 November 2016. See Alastair HENDERSON and Daniel WALDEK, “Singapore Arbitration Update: Third Party Funding and New SIAC Rules 2016”, Herbert Smith Freehills Arbitration Notes (1 July 2016).
82 Article 5B(1) of the Act to amend the Civil Law Act (Chapter 43 of the 1999 Revised Edition) and to make a related amendment to the Legal Profession Act (Chapter 161 of the 2009 Revised Edition), passed 10 January 2017 and assented by the President on 3 February 2017 (“Civil Law (Amendment) Act 2017”).
83 Ibid.
respondent-side funding, as well as BTE and ATE insurance that is not offered through a third-party funding agreement.

The relatively narrow scope of the Singapore definition of a third-party funding contract appears to be confirmed in the explanation in the draft version of the Bill regarding funder obligations required for enforcement of their rights under the funding contract. In its final version, Article 4 of the Civil Law (Third-Party Funding) Regulations of 2017 defines a third-party funder as an entity that “carries on the principal business, in Singapore or elsewhere, of the funding of the costs of dispute resolution proceedings to which the Third Party Funder is not a party.”

In a similar vein, Hong Kong recently enacted legislative reforms to permit third-party funding arrangements that were previously prohibited under the doctrines of champerty and maintenance. Under the Hong Kong Ordinance, like the Singapore legislation, “third-party funding” and the “funding agreement” are defined terms, but the Hong Kong legislation also defines separately “third-party funding.” Specifically, in defining funding, Section 98I of the Hong Kong Ordinance provides:

Third-party funding of arbitration is the provision of arbitration funding for an arbitration—
(a) under a funding agreement;
(b) to a funded party;
(c) by a third-party funder; and
(d) in return for the third-party funder receiving a financial benefit only if the arbitration is successful within the meaning of the funding agreement.

(2) However, third-party funding of arbitration does not include the provision of arbitration funding directly or indirectly by a person practising law, or providing legal services, whether in Hong Kong or elsewhere.

Notably, the definition precludes funding by attorneys in the same case in which they are acting as legal representatives, meaning that Hong Kong legislators intentionally excluded contingency fee arrangements from their definition of third-party funding. Hong Kong regulatory authorities are separately considering whether and how to enact reforms that would permit contingency fee representation.

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84 This limitation is confirmed in the Law Society of Singapore, Guidance Note 10.1.1, which describes “Third-party funding” as involving “a commercial funder agreeing to pay some or all of the claimant's legal fees and expenses.”

85 The exclusion in the Singapore Act definition of BTE and ATE insurance is likely related to the fact that the starting point for the legislative effort was to abolish the tort of maintenance and champerty, and these types of funding historically have not been regarded as implicating that tort.

86 See Article (4) the Civil Law (Amendment) Bill of 2016, and see Explanatory Statement of the Civil Law (Amendment) Bill of 2016.

87 See Article (4) of the Civil Law (Third-Party Funding) Regulations 2017.
Under the Hong Kong legislation, a “third-party funder” is defined in 98J as follows:

(1) A third-party funder is a person—
   (a) who is a party to a funding agreement for the provision of arbitration funding for an arbitration to a funded party by the person; and
   (b) who does not have an interest recognized by law in the arbitration other than under the funding agreement.

(2) In subsection (1)(b), the reference to a person who does not have an interest in an arbitration includes—
   (a) a person who does not have an interest in the matter about which an arbitration is yet to commence; and
   (b) a person who did not have an interest in an arbitration that has ended.

Under this definition, key aspects of the definition of a third-party funder is someone who enters into a funding agreement and does not have “an interest” either in “the matter” of an arbitration yet to be commenced or in “an arbitration that has ended.” The reference to an interest in “an arbitration” presumably means an interest in the substance of the underlying dispute. This definitional approach contrasts with the approach of the International Bar Association, which rests on a “direct interest” in the award.

In a separate Section 98H, the Hong Kong Ordinance defines the “funding agreement,” as follows:

A funding agreement is an agreement for third-party funding of arbitration that is—
   (a) in writing;
   (b) made between a funded party and a third-party funder; and
   (c) made on or after the commencement date of Division 3.

To date, the legislative efforts by Singapore and Hong Kong to regulate third-party funding is unique in their effort to regulate third-party funding in international arbitration. One reason is that these jurisdictions were later than many others in relaxing their prohibitions against maintenance and champerty. Only a few other jurisdictions have expressly regulated litigation funding in domestic contexts.

In England and Wales, in January 2014, a voluntary Code of Conduct for Litigation Funders (Code) was published by the Association of Litigation Funders. Because it pertains

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primarily to domestic litigation, it refers to “litigation funding,” even if that definition includes arbitration. Specifically, the Code provides:

“Litigation funding is where a third party provides the financial resources to enable costly litigation or arbitration cases to proceed. The litigant obtains all or part of the financing to cover its legal costs from a private commercial litigation funder, who has no direct interest in the proceedings. In return, if the case is won, the funder receives an agreed share of the proceeds of the claim. If the case is unsuccessful, the funder loses its money and nothing is owed by the litigant”.  

This definition is similar to the older version of the Code published in 2011. Notably, like the Singapore definition, it is limited to commercial funders. This focus is not surprising given the composition of the group that drafted it. This definition notably refers only to non-recourse funding of individual cases, and thus excludes many forms of funding that have been introduced since 2011.

As various institutions and entities have undertaken to assess issues that may arise with the participation of funders, and/or develop guidance or regulations relating to those issues, each institution or entity will have to base its analysis and final outputs on a definition. For this reason, it anticipated that the range of definitions presented in this Part will continue to expand.

B. Bi-Lateral Investment Treaties and Free Trade Agreements

In contrast to national legislation focused on commercial funders and claim-side non-recourse funding, definitions developed by international bodies have tended to adopt broader definitions. For example, certain several investment treaties and free trade agreements have introduced provisions addressing third-party funding, which adopt significantly broader definitions.

The draft European Union-Vietnam Free Trade Agreement was the first investment agreement to include a reference to, and purport to regulate, third-party funding.

Specifically, Article 2 of the draft EU-Vietnam Free Trade Agreement provides that:

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“Third Party funding” means any funding provided by a natural or juridical person who is not a party to the dispute but who enters into an agreement with a disputing party in order to finance part or all of the cost of the proceedings in return for a remuneration dependent on the outcome of the dispute or in the form of a donation or grant.”

The above definition is similar to the definition included in the European Union’s proposal for Investment Protection and Resolution of Investment Disputes under the Transatlantic Trade and Investment Partnership (TTIP). To that effect, Article 1 of Section 3 provides that:

“Third Party funding” means any funding provided by a natural or legal person who is not a party to the dispute but who enters into an agreement with a disputing party in order to finance part or all of the cost of the proceedings in return for a remuneration dependent on the outcome of the dispute or in the form of a donation or grant”.

Similarly, the revised version of the Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union adopted an explicit definition of third-party funding. Article 8.1 provides that:

“third party funding means any funding provided by a natural or legal person who is not a party to the dispute but who enters into an agreement with a disputing party in order to finance part or all of the cost of the proceedings either through a donation or grant, or in return for remuneration dependent on the outcome of the dispute”.

As one commentator notes, the CETA define “a not-for-profit funder by focusing on whether the funder expects repayment for the capital it advances to the funded party rather than focusing on what other motivations the funder might have besides profit.” In drawing this distinction, the CETA definition extends only to pro bono funding arrangements that contemplate reimbursement. In that author’s view, “[t]his definition is an appropriate catch-all, since the variety of motivations a funder could have may be endless.” According to one Member on the Task Force, the CETA definition would not extend to BTE insurers because their remuneration, in that Member’s perspective, is not dependent on the outcome of the dispute and the definition does not include the word “premium” in addition to “grant or donation.”

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92 See Article (2) of Chapter 8 of the [draft] EU-Vietnam Free Trade Agreement, January 2016.
93 See Article (1) of Section (3) of the European Union’s proposal for Investment Protection and Resolution of Investment Disputes under the Transatlantic Trade and Investment Partnership, dated 12 November 2015.
During its work, the Task Force benefitted from previews of draft bi-lateral investment treaty provisions regarding third-party funding, which included definitions of third-party funders. For example, a draft French Model BIT provides that:

“third party funder means any natural or legal person other than the disputing party who supports part or all of the costs of the arbitration in return for remuneration as a percentage of the compensation awarded by the tribunal entrusted to settle a dispute between an investor and the recipient host state of the investment of this investor.”

Meanwhile, a Draft Slovak Model BIT provides:

“A request for consultations must contain identification of any government, person or organization that has provided or agreed to provide any financial or other assistance to the investor in connection with the claim, or has an interest in the outcome of the claim.”

The final versions of these Model BITs are not publicly available and research has not identified other BITs that include specific language regarding third-party funding.

C. Arbitral Institution Rules and the IBA Guidelines

1. The IBA Guidelines on Conflicts of Interest

Before any arbitral institution took up the issue of third-party funding, the Task Force revising the 2014 IBA Guidelines on Conflicts of Interest sought to address the issue and adopted an expansive definition of funders. Specifically, General Standard 6(b) includes a requirement that arbitrators disclose the following relationships:

“[...] direct or indirect, between the arbitrator and the party (or another company of the same group of companies, or an individual having a controlling influence on the party in the arbitration), or between the arbitrator and any person or entity with a direct economic interest in, or a duty to indemnify a party for, the award to be rendered in the arbitration.”

The Explanation to General Standard 6(b) defines “third-party funder” or “insurer” as:

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“[…] any person or entity that is contributing funds, or other material support, to
the prosecution or defence of the case and that has a direct economic interest in, or
a duty to indemnify a party for, the award to be rendered in the arbitration.”

Reading the two provisions together, although General Standard 6(b) does not include the
requirement that the entity “is contributing funds, or other material support, to the prosecution or
defence of the case,” it would appear the two are meant to be read together. Under this reading,
the definition in General Standard 6(b) is limited by the additional language in the definition in the
Explanation to 6(b).

To date, no reported cases have adopted or provided clarification of the definition of third-
party funding including in the IBA Guidelines. Debate existed on the Task Force, similar to debates
noted above, about the extent to which the IBA definition extends to ATE and BTE insurance. In
addition to the arguments raised above, some Task Force members were of the view that the
requirement that there be a “direct economic interest” precluded this definition from applying to
ATE or BTE insurance. This view hinges on the observation that ATE and BTE insurers do not
have a direct claim to proceeds from an award. Instead, for example, BTE insurers were said not
to be entitled to “remuneration” since any amounts they receive would be in the form of premiums
paid. Consequently, it was argued, BTE insurers cannot be said to have a “direct economic
interest” in the award.

Others were of the view that this analysis was unduly formalistic and elevated form over
substance. Under this latter view, BTE insurers have the potential to receive recompense only in
the event of a favourable costs award, which would satisfy the requirement that they have a “direct
economic interest” in the award.

2. Arbitral Institutions

Mostly institutional rules do not include any provisions explicitly defining or addressing
third-party funding, with only a few exceptions.97

The first exception is the Brazilian CAM-CCBC, which in Administrative Resolution No.
18 of 20 July 2016 provides in Article 1:

“It is considered third-party funding when a natural or legal person who is not party to the
arbitration proceedings provides full or partial resources to one party so as to enable or assist the

97 See Aren GOLDSMITH and Lorenzo MELCHIONDA, “The ICC’s Guidance Note on Disclosure and
payment of the arbitration costs, receiving in return a portion or percentage of any profits earned from the award or from the agreement.” 98

The second exception, apparently adopted in response to the new legislation in Singapore, is a practice note adopted by the Singapore International Arbitration Centre in 31 March 2017. 99 The note addresses arbitrator conduct in cases involving “External Funding.”100 The note includes the following relevant definitions:

“‘External Funder’ means any person, either legal or natural, who has a Direct Economic Interest in the outcome of the arbitration proceedings”

“‘Direct Economic Interest’ means an interest in the arbitration proceedings resulting from the provision by a non-Disputant Party to a Disputant Party of funding for or indemnity against the award to be rendered in the arbitration proceedings”

These definitions appear broad enough to include both liability, and BTE and ATE insurance, though for reasons discussed above, there was some debate on the Task Force about whether the requirement that there be a “direct economic interest” might exclude ATE insurance from this definition. Notably, this SIAC practice note appears to be broader than the definition in Singapore legislation, discussed above.

Also in Singapore, the new SIAC Investment Arbitration Rules of 2017 provide in Article 24 that the arbitral tribunal have the power to

“order the disclosure of the existence of a Party’s third party funding arrangement and/or the identity of the third-party funder and, where appropriate, details of 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”.101

Notably, the SIAC Investment Arbitration Rules do not include a specific definition of third-party funding.

Also recently, the Singapore Institute of Arbitrators released its “Guidelines for Third Party Funders,” which describe third-party funding as follows:

“Third party funding arises when a third party (the Funder) provides financial support to enable a party (the Funded Party) to pursue or defend an arbitration or related court or mediation proceedings. Such financial support is provided in

100 Ibid.
exchange for an economic interest in any favourable award or outcome that may ensue.”

The SIArb Guidelines are presumed to be based on the London Association of Litigation Funders’ Code of Conduct. Under this view ATE insurers have an economic interest in a favourable award, but as described above, they do not provide financial support, only protection against a financial risk. For this reason, it appears that the SIArb Guidelines do not extend to ATE insurers, though it may apply to funders who also provide ATE insurance as part of a larger funding arrangement.

The ICC Guidance Note for the disclosure of conflicts by arbitrators endorsed a similar description of third-party funding, alongside ATE and liability insurers. The Note provides that arbitrators should consider, when evaluating whether to make disclosures, “Relationships between arbitrators, as well as relationships with any entity having a direct economic interest in the dispute or an obligation to indemnify a party for the award, should also be considered in the circumstances of each case.”

Finally, the China International Economic and Trade Arbitration Commission Hong Kong Arbitration Center (CIETAC) issued for public consultations guidelines for third-party funding in arbitration.

For the purposes of the guidelines, third-party funding was defined as:

“third party funding (“Funding”) arises when a professional third person or entity (“Funder”) contributes funds, or other material support to a party in arbitration (“Funded party”) and has a direct economic interest in the award to be rendered in the arbitration”.

While these are the first institutions to directly address the participation of third-party funders, other institutions—most notably ICSID—are working to follow suit.

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D. Arbitration literature

Several scholars have also attempted to define third-party funding. As is discussed below, some commentators adopt a narrow definition of the concept, while others adopt a broader definition.

Generally, those who adopt a narrow definition of third-party funding often generally limit their definition to the funding of arbitration cases by specialized funders who are not connected to the dispute and who provide funding in return for a potential profit.\(^{106}\)

Yves Derains defined third-party funding as:

“a scheme where a party unconnected to a claim finances all or part of one of the parties’ arbitration costs, in most cases the claimant. The funder is then remunerated by an agreed percentage of the proceeds of the award, a success fee, or a combination of the two or through more sophisticated devices. In the case of an unfavourable award, the funder’s investment is lost”.\(^{107}\)

Another scholar noted that:

“Third-party funding can be defined as the financing of an arbitration by a party who has no pre-existing interest in the dispute, usually on the basis that, if the funded party is successful in the dispute, the funder will be paid out of the proceeds of any amounts recovered as a consequence of the dispute, often as a percentage of the recovered amount”.\(^{108}\)

Third-party funding in the context of investment arbitration has been defined as follows:

“a contract between a claimant in an investment arbitration procedure and a party who has no pre-existing interest in the arbitration. The TPF funder will bear specific parts of the claimants’ out-of-pocket expenses concerning arbitration. The claimant will share a portion of the proceeds of the award or settlement with the funder. However, the funder is not


\(^{107}\) See Yves Derains, “Foreword to Third-Party in International Arbitration”, in Bernardo M. Cremades and Antonias Dimitritsa (eds), Third-Party Funding in International Arbitration, (ICC Dossier 2013), p. 5.

\(^{108}\) See Catherine A. Rogers, Ethics in International Arbitration, (OUP 2014) p. 182.
entitled to remuneration should the claim fail. Additionally, the TPF funder may agree to (in whole or part) indemnify the claimant for adverse cost orders”.109

In her monograph, Victoria Sahani Shannon defines third-party funding as:

“a financing method in which an entity that is not a party to a particular dispute funds another party's legal fees or pays an order, award, or judgment rendered against that party, or both. The agreement between the funder and the funded party may also include paying another party's attorney fees if the funded party loses the case or the decision-maker (i.e., an arbitrator or panel of arbitrators, a judge or panel of judges, or a jury) orders the funded party to pay the attorney fees of another party.”110

The inclusion of payment of an order or award may suggest that this definition includes insurance but, if so, it is not clear, from this wording, what type(s) of insurance the authors had in mind.

Another commentator has defined third-party funding:

“in general terms, third party funding involves a commercial funder agreeing to pay some or all of the claimant’s legal fees and expenses associated with a dispute in return for reimbursement of the funder’s direct outlays and a share of any sum recovered from the resolution of the claim (whether following settlement, judgment or award)”.111

A similar definition was used in another note:

“third party funding, also known as ‘litigation finance’, represents an alternative means to fund your claim. In simple terms, a commercial fund with no prior connection to the case – the ‘third party’ – finances the costs of the proceedings in return for a share of any damages awarded”.112

Similarly, in the context of litigation, scholars note that it third-party funding is:

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“The funding of litigation by a party who has no pre-existing interest in the litigation, usually on the basis that (i) the funder will be paid out of the proceeds of any amounts recovered as a consequence of the litigation, often as a percentage of the recovery sum; and (ii) the funder is not entitled to payment should the claim fail.”\textsuperscript{113}

Other commentators have defined third-party funding as follows:

“[…] an arrangement where a party involved in a dispute seeks funding from an outside entity for its legal representation. The outside entity—a third-party funder—finances the party’s legal representation in anticipation of making a profit. The third-party funder could be a bank, hedge fund, insurance company, or some other entity or individual. If the funded party is the plaintiff, then the funder contracts to receive a percentage or fraction of the proceeds if the plaintiff wins the case. Unlike a loan, the funded plaintiff does not have to repay the funder if it loses the case or does not recover any money. If the funded party is the defendant, then the funder contracts to receive a predetermined payment from the defendant, similar to an insurance premium, and the agreement may include an extra payment to the funder if the defendant wins the case”.\textsuperscript{114}

Third-party funding has also been defined as:

“A system by which one of the parties’ arbitration costs is being financed by a third-party to the arbitration proceedings, partially or in totality. In case of a favourable award, the third-party funder is generally paid by a previously agreed percentage of the proceeds of the award; however, in this context, third-party funding is a non-recourse loan, and in case of an unsuccessful claim, the claim-holder does not have to repay the funder”.\textsuperscript{115}

As noted by Jennifer Trusz:

“The third-party funding relationship involves a contract between the third party funding corporation and the claimholder. The funder provides money to allow the claimholder to pursue the claim in exchange for a share of a successful claim, whether by settlement, a court’s judgment, or an arbitrator’s award. After being reimbursed for its costs, the funding corporation generally receives between one-third and two-thirds of the claim. As a non-recourse loan, however, the claimholder does not have to repay the third-party funder for its investment if the claim is unsuccessful.”\textsuperscript{116}

On the other hand, other scholars have endorsed a rather broad definition of third-party funding; a definition that includes other financing agreements as well. Thus, some described it as “every possible contract where the pay-out under that contract is linked to the proceeds of litigation”. While this definition necessarily includes third-party funding, it also includes lawyers’ contingency fee arrangements and insurance contracts, even though they are held by different stakeholders. The purposes of such a broad definition are numerous, but primarily to facilitate systematic study of funding alternatives that are functionally similar and to arrive at insights and recommendations that are fair and rational.

A similarly broad definition of third-party funding has been suggested by other commentators to the effect that:

“In its broadest definition, TPF is the funding of the costs of bringing or defending a claim by a party which is not itself a party to the arbitration. This would include funding by insurers, such as ‘before the event’ and liability insurers, who regularly stand behind parties in commercial arbitrations.”

In this regard, others have suggested that third-party funding should be distinguished from other related financial agreements. Proponents of this position argue that BTE and liability insurers differ from non-recourse third-party funding both in the level of control exercised over the dispute and in the applicable industry and ethical rules applicable to each.

Notably, many of the above definitions adopted by scholars are limited to funding of individual cases on a non-recourse basis. In this respect, it is worth noting that even the passing of a few years, in which the market for funding has become much more complex and the forms of funding more diverse, scholarly definitions will likely expand to address these changes.

V. Functional considerations related to the definitional task

Given difficulties in defining third-party funding in conceptual terms, this Part examines functional and comparative aspects of funding that may be helpful in assessing alternative definitions. This functional approach aims to move beyond formal definitions to determine the key functions of different forms of funding in order to focus on those functions that are unique or

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not unique to third-party funding.

By identifying specific types of conduct, rather than categories of actors, a functional or conduct-based approach may help focus definitional questions can avoid development of overbroad standards, guidelines or rules, and facilitate more nuanced analysis to distinguish between conduct in which funders’ activities do not raise issues that are the target of such rules and guidance. Alternatively, functional similarities between third-party funding and other types of finance may provide a basis for extending existing rules or doctrines that apply to other actors, such as the extension of the common interest privilege from the insurance industry to third-party funding.

A. Assessment and Risk-Assumption

One important benefit third-party funders bring to dispute settlement is an ability to engage in a disinterested, dispassionate and highly detailed assessment of claims. This function differentiates them from both the client and its attorney. A client, no matter how sophisticated, may be influenced by business incentives and perceptions about the facts underlying the claim. Meanwhile, a party’s lawyers may, intentionally or unintentionally, be influenced both by an effort to please a client interested in bringing a claim as well as their own potential to earn hourly fees. By contrast, funders and traditional insurers have both structural detachment and financial incentives to engage in a uniquely independent incentive to assess cases, and by many reports that leads to extensive, fine-tuned assessment of the case.

Leading funders report an average review-acceptance rate of 10-1, meaning that for every 10 cases reviewed, they only agree to fund one case.\footnote{Cento VELJANOVSKI, “Third-Party Litigation Funding in Europe” 420, available at <https://www.researchgate.net/publication/228120796_Third_Party_Litigation_Funding_in_Europe> (last accessed 19 August 2017).} In deciding whether to accept a case, they assess its legal, factual, practical, temporal, and (sometimes) political variables to determine risks, likelihood of success, and potential rate of return. With the exception of the rate of return, BTE insurers undertake a very similar process. In making this assessment, funders are free from many of the pressures that can cloud a party’s or law firm’s assessment of the same claim. They are also subject to pressures from shareholders to pick claims that are likely to deliver high rates of return.
In assessing claims, some argue that funders bring a level of sophistication and precision unique even among large, sophisticated multi-national companies and law firms, though there have also been anecdotal reports of inadequate due diligence or inaccurate case assessments.

As described in Chapter 1, third-party funders generally create a risk-assessment model or matrix that takes into account the percentage likelihood of different outcomes in light of specific factors. These factors include, among others, the jurisdiction of the claim, strength of the claimant’s legal arguments, strength of facts supporting the arguments, extent of loss flowing directly from the respondent’s conduct, a claimant’s motivation, commitment and honesty, the experience of the claimant’s legal team, the respondent’s ability/likelihood to pay, reasonable duration to obtain an award, and costs of bringing the claim.

Data for the matrix is obtained through due diligence by the funder, its legal team, and accountants (and other experts, such as intelligence and data recollection). The analysis entails inquiries of the claimant’s lawyers regarding timing and evidentiary issues, legal strategy, and compilation and assessment of material documents. Importantly, conducting this kind of due diligence often requires assessment of confidential information. Based on this matrix, the funder determines the likelihood of estimated returns on investment over a period of years, which will be weighed against other investments in the funder’s overall portfolio.

The extent of funders’ due diligence in comparison insurance with is ultimately an empirical question and may vary among funders (or insurers), and from case to date. For the purposes of assessing definitions, however, the fact that most insurers (most notably BTE insurers) undertake similar due diligence confirms that case assessment is not new or unique to modern third-party funders, and indeed may be considered an essential predicate for any entity contemplating assuming risk tied to the outcome of a particular case. In the insurance context, the need for case assessment is in part what has led to development of the so-called “Common Interest Privilege.” The similarities in case assessment by funders and insurers if part of the basis for arguments that the same privilege that applies to confidential communications with insurers should

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123 In the Task Force’s final report, this Report on Definitions will be preceded by a chapter/report that provides an overview of the mechanics of third-party funding.


125 The Task Force did not pursue empirical research on this topic, but future empirical research on this issue may be useful.
extend to third-party funding, a topic taken up in Chapter 5.

It is uncertain the extent to which these case assessment procedures are as rigorous when cases are financed as part of a portfolio. “Portfolio financing” is a relatively new model that may challenge some of these basic features of conventional third-party funding. As one funder describes, “the portfolio approach is inherently flexible and ideally suited for defensive matters as well as claims, and for matters that would otherwise be less attractive for funding. Pricing is generally lower because risk is diversified.”

Diversifying risk may make initial assessment of risk less essential. As a consequence, it is at least plausible that the assessment criteria are diluted when investment is made in numerous cases contained in a portfolio, which are designed to spread the risk of higher risk investments.

In portfolio financing, the rationale seems to be similar to contracting risks in the insurance industry. Indeed, in the words of one author, the “practice has shown that the losses can be offset by the wins across the board and as long as the value of the winning cases is greater than the amount expended on a losing case, the funder will make a profit.”

Similarly, spreading the risk in terms of volume and quantity reduces the negative consequences of an unsuccessful portfolio. In this sense, a funder may well provide funds for twenty or more cases at a time, each of them with different chances of success and different amounts at stake. The funder may anticipate that it will likely lose some of those cases, but considers the overall investment will likely be worthwhile if the success taken in a sufficient number of cases to render the overall portfolio profitable. At the same time, a loss incurred in a case will be unlikely to affect the performance of the portfolio as a whole.

With portfolio funding, because the rationale of the risk underlying this investment becomes statistically spread across the portfolio, funders’ assessment of cases may in practice be less rigorous than in individually selected cases for one-off funding. Similarly, funders may exert a lesser degree of control over individual cases when funding on a portfolio model.

Burford Capital appears to be the pioneer in this business model, though it is unclear the extent to which its portfolio funding involves international arbitrations, as opposed to domestic litigation. No evidence has come to the attention of the Task Force, as of the date of this publication, of other funders actively engaging in portfolio funding in international arbitration, apart from anecdotal evidence of defence side portfolio funding of States in investment arbitration.

To the extent portfolio funding becomes more prevalent, it may require reconsideration of issues relating to how cases are assessed for funding. If assessment (and control) are minimized in

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127 See Nick ROWLES-DAVIES, Third-Party Litigation Funding (OUP 2014) p. 72.
certain types of portfolio funding, it may be that that funding model more resembles other forms of passive corporate financing that do not implicate certain issues implicated in third-party funding of individual cases.

B. Control & Cost-Containment

Another functional consideration that may affect whether or how to regulate third-party funding is the level of control that a funder may exercise over case strategy, particularly in its efforts to control costs. Control over case management is not viewed by the Task Force as either an inherently good or bad feature of funding, but it may be relevant in evaluating certain issues how similar modern third-party funding is to other means of dispute financing, which may in turn affect analysis of certain issues, such as disclosure and conflicts.

In some jurisdictions, the exercise of control by a funder—particularly over a case’s larger objectives like settlement—can also raise ethical issues for counsel. As national ethical rules vary considerably both on whether and how they regulate these issues, the Task Force did not consider or endeavour to articulate any guidance about attorney obligations in light of funder control. As examined in Chapter Seven on Best Practices, the extent, nature, and conditions of control are largely a function of the funding agreement negotiated by the party and funder, applicable law, and, in some jurisdictions, applicable ethical or industry rules.

Although the Task Force does not make any recommendations regarding the appropriateness of funder control, an understanding of the functional aspects of a funder’s control can be an important touchstone in assessing the degree to which third-party funding is similar to or different from other types of dispute financing. Unfortunately, there are inconsistent reports and no empirical evidence regarding the actual degree of control that funders exercise over management of a case. Some funders report that, after careful initial assessment, they function only as distant and detached monitors who are entitled to receive regular updates.129 Other anecdotal reports indicate that, on more than one occasion, a third-party funder has directly appointed an arbitrator or physically appeared at an arbitral hearing.

Meanwhile, some argue that a relatively high degree of control would be important for funders to be able to protect their investment and ensure that a case is prosecuted consistent with the assumptions and analysis that facilitated the funding in the first place. This view has effectively been endorsed by the Court of Appeal in England, which reasoned that a third-party funder’s “‘rigorous analysis of law, facts and witnesses, consideration of proportionality and review at appropriate intervals’ is what is to be expected of a responsible funder.”130

129 Jonathon MOLOT, “Theory and Practice in Litigation Risk”, “Burford has no control over litigation or settlement decisions and it does not interfere with the attorney client relationship.”, available at <http://rippmedia.com/Molot-TheoryandPractice.pdf> (last accessed 15 August 2017)

130 Excalibur Ventures v Texas Keystone and others [2016] EWCA Civ 1144.
Consistent with this view, third-party funders may control or exercise detailed oversight over numerous strategic decisions in a case, including arbitrator selection, expenditure of significant funds (such as retention of experts), changes in legal teams, drafting of memoranda, oral pleadings, and settlement. The extent to which any particular funder in any particular case exercises all or some of these controls will depend on internal practices and protocols of the funder, the nature of the case, the professional relationship the funder has with the funded party and legal team, the financial terms in the funding agreement (which may include financial incentives that reduce the need for monitoring), as well as specific provisions in the funding arrangement that either expressly authorize or limit certain forms of control.

Termination rights also factor into concepts of control. As von Goeler explains:

“when some major litigation funders emphasise in their webpages that they do not control cases, perhaps what they mean is that such express contractual rights to veto specific decisions tend to be absent. However, to what degree a litigation funder will be able to exercise control over the conduct of a claim is not only determined by the existence or not of express veto rights over key decisions. This will also depend on the funder’s termination rights and, not least, on the configuration of the litigation funder’s case monitoring.”131

In some respects, the control exercised by third-party funders similar to the control exercised by insurance companies. As Charles Silver describes:

“Liability insurers manage quality and cost ruthlessly and creatively. They make defense-related decisions directly, thereby obtaining complete freedom to use their vast experience dealing with lawyers to minimize litigation costs. They decide which lawyers to hire, obtain volume discounts by concentrating work in a small number of firms, maintain staff counsel operations in areas where the volume of work is sufficient to justify the expense, subject lawyers to litigation management guidelines and audits, and use innovative fee arrangements to motivate outstanding performance. Insurers also control settlement negotiations and decision making. This enables them to act on their incentive to minimize costs by deploying their knowledge of claim values with maximum effect.”132

The similarities between the control exercised by third-party funders and insurers are often treated as relevant to various questions regarding whether and how to regulate third-party funders. For example, the “common interest privilege” that applies to insurers in some common law jurisdictions is often pointed to as a basis for extending attorney-client privilege to third-party funders.

The comparison between funders and insurers is also raised with respect to issues of disclosure. For example, in many jurisdictions, such as the United States, the presence of an insurer in a case is required to be disclosed, but the fact that a party is insured may not be

132 SILVER, p. 621-22.
considered in assessing the damages to be awarded. Although legislative reforms have not yet extended the disclosure rules to third-party funders in the United States, the similarity in their function may be the reason why disclosure of third-party funding is required in some contexts in Australia, England, and New Zealand.

Shipowners’ and Defence Clubs are excluded from any recommendations or guidance provided by the Task Force as part of the carve-out of maritime arbitration, identified above. They are, however, an interesting point of reference in discussions of control over funded cases.

Shipowners’ and Defence Clubs exercise discretion over whether to provide their members with funding for litigation or arbitration, leaving the decision to club managers or boards. For example, usually Shipowners’ Club rules allow the club’s managers to appoint lawyers on behalf of their ship-owner members. For example, Rule 6 of the UK Shipowners’ Club Rules 2015 provides:

“All persons appointed by the Association on behalf of the Member or appointed by the Member with the approval of the Association shall be or be deemed to be appointed on the terms that they have been instructed by the Member at all times (both while so acting and after they have ceased so to act): (a) to give advice and to report to the Association in connection with the claim, dispute or Proceedings; (b) to seek and act on the instructions of the Association; and (c) to produce to the Association any documents or information in their possession or power relating to the claim, dispute or Proceedings, as if such persons had been appointed to act and had at all times been acting on behalf of the Association.”

133 See Chapter 1, p. 6.


Shipowners’ Clubs may also provide a cap for maximum recovery amounts, and can further require members to contribute to the costs of all legal expenses should they pass beyond a specified threshold.

Clubs exercise decision-making control throughout arbitral proceedings they fund, typically requiring either that members’ lawyers follow the club’s instructions or that members to use lawyers chosen by the club. “Unlike other forms of legal expenses insurance (which FD&D cover largely predated), the Club’s managers (who are often qualified lawyers) remain involved with the day-to-day handling of the case, with the assistance of external lawyers where necessary.”

Regarding the insured’s right to select their own lawyers, an exemption in the English Insurance Companies (Legal Expenses Insurance) Regulations 1990 provides that its provisions ensuring the insured’s right to select its own lawyers do not “apply to legal expenses insurance contracts concerning disputes or risks arising out of, or in connection with, the use of sea-going vessels.”

In contrast to both third-party funding and insurance, with attorney financing (most typically through contingency-fee arrangements), control in theory remains with the client. This assumption exists despite the fact that the attorney is assuming most or all of the risk of the client losing the case and despite the fact that in class action cases, the clients may have little at stake in the case in comparison to the attorneys.

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Attorney financing, usually through a contingency fee arrangement, is another context in which an entity that is not an original party to the underlying lawsuit may nevertheless exercise a degree of control over certain aspects of the proceedings as a means of protecting. When they lawyers or law firms represent parties on a contingency fee basis, they are also in a position to exert control over aspects of the dispute.

In those jurisdictions that permit contingency fee arrangements, applicable codes of conduct and professional ethical rules generally require attorneys to be loyal to their clients, even in the face of their own competing interests. In the United States, courts also operate as a check on attorneys in contingency fee, class action cases. Notably, some third-party funding agreements include contingency fee arrangements with law firms providing representation. For those agreements, the funding arrangement may be subject to attorneys’ ethical rules, in addition to contractual provisions between the parties or other applicable legal rules.

VI. Overview of Definitions Used in Subsequent Chapters

As noted above, the Working Definition of the Task Force is intentionally broad to facilitate consideration of all types of third-party funding. For the purposes of discussion and study, this broad Working Definition facilitated analysis of functional similarities among different financing options, and their increasing overlap and integration in the market for litigation finance.

While comprehensive consideration of the range of options was important for discussion, such a broad definition is not necessarily helpful for assessing certain technical issues. For example, the insurance industry, insurance markets, and the participation of insurers in national court proceedings are already generally regulated through national insurance and financial regulations, through national procedural rules (in the litigation context), and through professional ethical regulations. Until recent revisions to the IBA Guidelines, and related reforms in Singapore and Hong Kong, insurers were not subject to disclosure and analysis with respect to conflicts of interest with arbitrators. For reasons examined in greater detail in Chapter Four, insurance is included in the Task Force definition regarding arbitrator conflicts of interest, but it is not included in definitions in other chapters.

Notably, it would be superfluous for Chapter Five, which addresses privilege, to include insurance as part of the definition of third-party funding. Chapter Five instead examines the so-called “common interest privilege” that exists for insurers in many jurisdictions and whether that privilege or the justifications for it should also extend to third-party funders.

Meanwhile, in Chapter Six, which addresses costs and security for costs, insurance is in some respects relevant to the analysis. For example, the existence of ATE insurance has, in at least one case, been the reason a tribunal denied a request for security for costs. Meanwhile, to the extent third-party funding may be considered in assessing whether to order security for costs, such
funding does not raise any questions different from those implicated by contingency fee arrangements.

Chapter Seven, which provides a compendium of best practices, addresses only modern third-party funding. As noted above, insurers’ relationships with their customers are already regulated through national legislation and attorney funding through contingency fees are regulated through domestic regulation of the legal profession.

For Chapter Eight, which addresses issues in investment arbitration, once again it is important to use a broad definition of third-party funding, which comprehends not only modern non-recourse funding, but also respondent-side funding, including by non-governmental organizations, but also those types of insurance that operate as functionally equivalents to modern funding and arguably raise similar issues.

VII. Conclusion

One of the challenges in recent debates about third-party funding, and related efforts to introduce related reforms, is that they often start with implicit assumptions about third-party funding, but without clear definitions of the phenomena that is the focus of their attention. As demonstrated in the analysis of this Chapter, certain definitions either include or exclude certain forms of financing that may or may not be intended for inclusion or exclusion. Accidental inclusion or exclusion of related phenomenon may raise questions about coherence and fairness.

It is hoped that the analysis in this Chapter, read together with Chapter Two, will illuminate aspects of the practice and market of third-party funding and facilitate deeper understanding, particularly in understanding the analysis in the Chapters that follow.
Chapter 4

DISCLOSURE AND CONFLICTS OF INTEREST†

PRINCIPLES

[ALTERNATIVE A]:

1. A party should, on its own initiative, disclose the existence of a third-party funding arrangement and the identity of the funder to the arbitrators and an arbitral institution or appointing authority (if any), either as part of its first appearance or submission, or as soon as practicable after funding is provided or an arrangement to provide funding for the arbitration is entered into.

[ALTERNATIVE B]:

1. Arbitrators and arbitral institutions have the authority to, during the selection and appointment process, expressly request that the parties disclose whether they are receiving support from a third-party funder and, if so, the identity of the funder.

[ALTERNATIVE A]:

2. For the purposes of the Principles in Chapter 3, the term “third-party funder” is defined as follows:

For the purposes of assessing potential conflicts of interest, the terms ‘third-party funder’ and ‘insurer’ refer to any natural or legal person who is not a party to the dispute but who enters into an agreement either with a disputing party, an affiliate of that party, or a law firm representing that party, in order to finance part or all of the cost of the proceedings, either individually or as part of a selected range of cases, and such financing is provided either through a donation or grant or in return for remuneration dependent on the outcome of the dispute.

[ALTERNATIVE B]:

2. For the purposes of the Principles in Chapter 3, the term “third-party funder” is defined as follows:

† Primary contributors of this Chapter include Victoria Shannon Sahani, Mick Smith, Stavros Brekoulakis, and Catherine Rogers.

* This Chapter presents alternative options for the Principles it articulates. These alternatives are based on continued differences that existed among Members of the Task Force and on which input during the public comment period is specifically sought.
For the purposes of assessing potential conflicts of interest, the terms ‘third-party funder’ refers to any natural or legal person who is not a party to the dispute but who enters into an agreement either with a disputing party, an affiliate of that party, or a law firm representing that party, in order to finance part or all of the cost of the proceedings, either individually or as part of a selected range of cases, and such financing is provided either through a donation or grant or in return for remuneration dependent on the outcome of the dispute. This definition does not extend to agreements that provide insurance or to persons who provide insurance.

3. In light of any disclosures made pursuant to Principle 1, above, arbitrators and arbitral institutions should assess whether any potential conflicts of interest exist between an arbitrator and a third-party funder, and the need to make appropriate disclosures or take other appropriate actions that may be required under applicable laws, rules, or Guidelines.
I. ANALYSIS

Potential conflicts of interest between third-party funders and arbitrators were among the first and most prominent issues that attracted attention with respect to their participation in international arbitrations. More specifically, questions have arisen as to the extent and nature of disclosures to be made to allow arbitrators, parties, and institutions to assess potential conflicts of interest involving funders. The Chapter proceeds in the following parts. Part 1 provides a general overview and delineates relevant background considerations. Part 2 considers the scope of the definition of third-party funding appropriate for the purpose of analyzing conflicts. In explaining the definition adopted by the Task Force, the analysis in Part 3 compares and contrasts other existing definitions, including those adopted by the International Bar Association (IBA) Guidelines on Conflicts of Interest in International Arbitration (IBA Guidelines), and other national and international sources. Finally, Parts 4 and 5 analyze, respectively, when disclosures need to be made and by whom, and the effect of unknown conflicts.142

1. Background

The potential for arbitrator conflicts of interest due to the involvement of third-party funders has garnered increasing attention for a number of reasons in recent years: the increase in the number of cases involving third-party funding, the highly concentrated segment of the funding industry that invests in international arbitration cases, the symbiotic relationship between funders and a small group of law firms, and relatedly, the often close relations among elite law firms and leading arbitrators.143 In addition, a number of leading arbitrators have taken positions within, or ad hoc consultant roles with, some funders.144 Against this backdrop, the potential for conflicts of interest for arbitrators in funded cases can materialize out of several possible scenarios.

The Principles and analysis in this Chapter are premised on the following background considerations:

142 These principles are subject to revision and have not yet been finally endorsed by the Task Force.
144 It was pointed out in Task Force discussions that arbitrators do not tend to take on such roles with traditional insurers.
1. The participation of a third-party funder in an international arbitral dispute can create the potential for a conflict of interest that should be disclosed by an arbitrator;
2. Knowledge of the participation of a third-party funder in international arbitral disputes is an essential predicate for arbitrators to make necessary disclosures;
3. Third-party funding may be provided through a variety of structures such that it is difficult to isolate a single definition of third-party funding;
4. Avoiding conflicts of interest is in the best interest of all parties and arbitrators, and is important for the legitimacy of international arbitration; and
5. Disclosure should strike an appropriate balance between providing adequate information for arbitrators, parties, institutions, and appointing authorities to assess potential conflicts of interest, but avoid excessive disclosure that may lead to unnecessary delay and significant expense from frivolous challenges to arbitrators, or unfounded applications for disclosure of financial information and funding agreements.

In light of these starting considerations, and based on analysis provided in greater detail below, broad agreement existed on the Task Force that disclosure by the funded party of the existence and identity of funders is necessary so that arbitrators could make appropriate disclosures and decisions regarding potential conflicts of interest. This view was regarded as keeping with global trends in regulation of third-party funding, which increasingly requires disclosure of the existence and identity of the entity providing funding. There was also general agreement on the Task Force that, absent exceptional circumstances, no other information except the existence and identity of funders was required for the purposes of analyzing conflicts of interest.

There was disagreement about whether that disclosure should be as a matter of course in every case [Principle 1, Alternative A], or based on a request for disclosure by the arbitrators [Principle 1, Alternative B]. The arguments for and against each of these positions are presented below.

The Task Force does not propose any new or special rules or guidelines regarding how potential conflicts between funders and arbitrators should be analyzed or when such potential conflicts should lead to recusal or disqualification. Instead, the Principles in this Chapter address only the issue of how and when disclosures should be made to enable arbitrators to make relevant assessments about potential conflicts of interest based on existing applicable standards and guidelines. It leaves to other sources—the IBA Guidelines, arbitral rules, and national legislation—the substantive analysis of potential conflicts.

2. Definition of Third-Party Funding for Conflicts Analysis
Until relatively recently, there was debate about whether it was possible for funders, or at least certain types of funding, to create conflicts of interest for arbitrators.\textsuperscript{145} Third-party funding, it has been argued, could not raise potential conflicts of interest because it is simply one among many possible forms of financial support for pursuing or defending a dispute. The source of financing for a dispute is irrelevant to the merits of the dispute, the argument goes, and there is no reason to treat third-party funding as subject to any special treatment that would not apply, for example, to a corporate loan taken out for the purpose of pursuing a claim.\textsuperscript{146}

Most opposition to disclosure is not so much a desire to keep secret the presence of funding or identity of the funder, but rather a reaction to the procedural and strategic consequences of disclosure, such as challenges to arbitrators and requests for security for costs. Some report a problem with frivolous arbitrator challenges based on alleged conflicts, and requests for security for costs that are based solely on the existence of funding, not a genuine risk that a potential cost award could not be satisfied.\textsuperscript{147} It was also suggested by some that these responses to disclosure may not simply be a matter of case strategy, but an intentional effort to drive up the cost of the case to make the funding model untenable.

Another argument against disclosure of funding arrangements for the purposes of assessing arbitrators’ potential conflicts of interest is that unknown conflicts of interest cannot be a basis for an effective challenge to an arbitrator or an award. Some arbitrators and courts have in fact found that unknown conflicts cannot be a basis for refusing enforcement of awards. Even though a resulting award may not always be subject to set aside or refused enforcement, however, there are other potential costs to undisclosed conflicts.

If an unknown conflict of interest relating to a third-party funder later comes to light, the result can be messy and expensive for the parties. Regardless of whether an arbitrator is removed or an award set aside or refused enforcement, the parties and the funder waste time and fees. Even a truly unknowing arbitrator may suffer the embarrassment of having his or her integrity questioned publicly, and potential harm to reputation even if vindicated on the merits. Finally, challenges based on undisclosed conflicts can undermine the integrity and legitimacy of international arbitration generally.

\textsuperscript{145} See, e.g., Christopher BOGART, (taking as a “given that “there is no legal, logical, or equitable basis for requiring disclosure of funding without also requiring the disclosure of other parties with economic interests in the outcome of a matter”). Arguably, this language could be interpreted to that no test for disclosure regarding funders could be valid unless it applied equally to all forms of economic interests, not only equity investors. This interpretation is consistent with his earlier assertions that ‘arbitration finance is really just specialty corporate finance’. See Mark KANTOR, “Third-Party Funding in International Arbitration” 24(1) ICSID Review - Foreign Investment Law Journal (2009) p. 65; Maya STEINITZ, “Whose Claim Is This Anyway?” 11-13 University of Iowa Legal Studies Research Paper (2011) p. 1268 at p. 1292.


\textsuperscript{147} For an extended discussion of standards for granting security for costs, see Chapter 2. For an extended discussion of competing views in the underlying policy debate, see Chapter 8.
Today, consensus has emerged in the international arbitration community that that the existence of third-party funding can raise potential conflicts of interest for arbitrators. Most on the Task Force supported mandatory disclosure of funding by the funded party as a matter of course during the arbitrator selection process or at the initiation of funding if after constitution of the tribunal.\[148\] This view finds some support in the results of the 2015 Queen Mary School of International Arbitration survey, in which 76% of survey respondents agreed that that disclosure of the existence of third-party funding should be mandatory, 63% believed that disclosure of the identity of the funders should be mandatory, and 71% that the full terms of the funding agreement should not be disclosed.\[149\]

However, the support for funding apparently expressed in the Queen Mary Survey may be subject to question since only 39% of those surveyed had experience with third-party funding in practice, and 9% were not even aware of it. The Survey also revealed support for the notion that systematic disclosure may make the use of funding a more routine part of arbitral dispute resolution.\[150\]

Others on the Task Force proposed that, instead of a general presumption of disclosure in every case, it is more prudent to confirm the authority of arbitrators and arbitral institutions to request disclosure of such information as needed. Support for this view is based on the prospect of disagreements between parties and funders about the effect of disclosure requirements in non-binding soft-law instruments, as opposed to mandatory compliance with a procedural order. These alternative approaches are explored in greater detail below. Consensus about the disclosure of funding for the purpose of assessing potential conflicts has raised related questions about what kinds of dispute financing should be included in the definition of “funding” or “funder” for the purposes of conflicts of interest analysis, and the means and process for disclosing funding.

The sources that govern potential arbitrator conflicts of interest are numerous, and include arbitral rules, national law, and international soft law instruments, such as the IBA Guidelines. Given that modern third-party funding is a relatively recent phenomenon, not many of these sources have specifically addressed the issue of potential conflicts of interest involving third-party funding.


\[150\] Notably, this survey, and related discussions in international arbitration, do not generally take account of practices in ad hoc and trade association arbitration, most notably in the maritime industry, which account for large numbers of arbitrations every year. These are among the reasons why this Report does not seek to address funding in maritime arbitration. See Chapter 1, at p. 6.
The IBA was the first organization to officially take a position in the third-party funding conflicts of interest debate by implementing the 2014 IBA Guidelines on Conflicts of Interest in International Arbitration (IBA Guidelines). The IBA Guidelines define third-party funders and insurers as relevant to conflicts analysis if they have a “direct economic interest” in an award. As examined in greater detail below, this definition still leaves unresolved some questions regarding the scope and application of the IBA Guidelines to certain types of dispute financing. The IBA definition has, nevertheless, been subsequently been adopted by the Singapore International Arbitration Centre in its Practice Note\(^ {151}\) and the 2 February 2016 Guidance Note on conflict disclosures by arbitrators” adopted by the ICC.\(^ {152}\) Other instruments, for example proposed Bilateral Investment Treaties and trade agreements, have adopted different, arguably broader definitions.

A. The IBA Definition

The 2014 IBA Guidelines provide in General Guideline 6(b) the following guidance with respect to the range of entities that should be considered in assessing potential conflicts of interest, which now includes reference to third-party funders:

“If one of the parties is a legal entity, any legal or physical person having a controlling influence on the legal entity, or a direct economic interest in, or a duty to indemnify a party for, the award to be rendered in the arbitration, may be considered to bear the identity of such party.”

This Guideline provides that any entity that has “a direct economic interest in, or a duty to indemnify a party for, the award to be rendered in the arbitration” may be treated as bearing the identity of the party for the purpose of assessing conflicts of interest.

The Explanation to General Standard 6(b) provides a definition, which includes additional details:

\(^{151}\) Singapore International Arbitration Centre Practice Note, PN—01/17 (Mar. 31, 2017), Administered Cases under the arbitration rules of the Singapore International Arbitration Centre, On Arbitrator Conduct in Cases Involving External Funding, Mar. 31, 2017, available at

“For these purposes, the terms ‘third-party funder’ and ‘insurer’ refer to any person or entity that is contributing funds, or other material support, to the prosecution or defence of the case and that has a direct economic interest in, or a duty to indemnify a party for, the award to be rendered in the arbitration.”

Importantly, the definition in Explanation for General Standard 6(b) includes the requirement that the funder be “contributing funds, or other material support, to the prosecution or defence of the case” in addition to the requirement that the funder have “a direct economic interest in, or duty to indemnify a party for, the award.” Nevertheless, neither General Guideline 6(b), nor its Explanatory Note, define “direct economic interest.” It is uncertain, therefore, whether this term would capture, for example, an indirect obligation to reimburse a party or payments that are not taken directly out of an award, but instead simply conditioned on a particular outcome, such in some forms of After-the-Event (ATE) insurance.¹⁵³

One view expressed on the Task Force was that reference to a ‘direct economic interest’ was too broad and vague because it could refer to any range of entities, including some not intended to be addressed. Under this view, it was suggested that instead the definition should be limited to an interest in proceeds or the prospect of making a profit in the event of success, and a definition should instead refer to a ‘return on investment’.

Notably, the IBA definition in the Explanation of General Standard 6 extends explicitly to “insurers.” For reasons elaborated below, for the purposes of analyzing potential conflicts of interest, insurers (whether liability insurers or before- or after-the-event insurers) can function similarly to funders and, thus, may raise some of the same issues as funders with respect to potential conflicts of interest.

As noted above in Chapter 3, the wording in the IBA Guidelines may not always extend to BTE insurers (because they arguably do not have a ‘direct economic interest’ in the outcome as their remuneration may consist in their payment of a premium paid in advance). One view on the Task Force was that this definition would likewise not extend to ATE insurers since it was doubted that their policies alone could be said to be providing ‘material support.’¹⁵⁴ On the other hand, the IBA definition does not appear to be broad enough to capture other types of funding that would seem to raise similar questions regarding potential conflicts of interest. For example, by focusing on “direct economic interests” in the award, the IBA Guidelines’ definition excludes funders that may have an interest in the award, but whose interest may not be considered a “direct economic” interest.¹⁵⁵

For example, in investment arbitration, non-profit organizations, third States, or other parties have provided funds or material support to a party. The purpose of these funds or support

¹⁵³ See Chapter 2 p. 24 (describing ATE insurance).
¹⁵⁴ See Chapter 2, p. 25.
¹⁵⁵ An argument was raised that this definition would encompass non-for-profit funding because such funding would imply a “moral obligation” to reimburse for value received, and that moral obligation would be sufficient to constitute a “direct economic interest” in the award.
is to increase the likelihood that an award will further a particular policy, or provide meaningful precedent which may, indirectly, promote their interests in the long term. For example, as Victoria Sahani explains:

“In Quasar de Valores SICAV S.A. et al. v The Russian Federation, SCC Arbitration No. 24/2007, Award of 20 July 2012, para. 223, the funder, Group Menatep Limited, was a former majority shareholder in the Russian oil company Yukos, rather than a separate third-party funding company, and there was no contract in place requiring the claimant to reimburse Menatep. By funding the Quasar de Valores case, Menatep was seeking to create a favorable ‘precedent’ in hopes that such a precedent would be applied in its future, much larger, shareholder dispute against Russia under the Energy Charter Treaty.”

Such participation even in the absence of a direct economic interest may nevertheless raise potential conflicts of interest with arbitrators in those arbitrations, but the existence of such funding would not be required to be disclosed under the IBA Guidelines’ definition because it is limited to a “direct economic” interest in the award.

In addition to ambiguities about whether the definition of “direct economic interest” in the IBA Guidelines extends to non-commercial funders or BTE insurers, it is also uncertain whether or to what extent the definition would address portfolio financing or law firm funding, where a loan is made to a law firm collateralized by anticipated income from identified cases. In law firm financing a funder provides financing directly to a law firm (not a party). The funding is provided usually based on a range of cases on which the law firm is counsel and in which the law firm may have a contingent or conditional fee arrangement. Portfolio financing may also be provided when a party has multiple arbitrations.

Portfolio funding for law firms allows funders to spread risk. It also means, however, that their compensation is not necessarily tied to the outcome of any individual arbitral award, but instead on the performance of the portfolio. Such funding is usually on a non-recourse basis, meaning that the funder’s recovery is still tied to the outcome of the arbitrations. As such, portfolio financing may be regarded as providing funders with an economic interest in the awards in the portfolio, but it is not certain that interest would be considered a “direct” or “indirect” economic interest in the award, such that portfolio funding would fall within the IBA Guidelines’ definition.

Nevertheless, even acknowledging the limitations of the definition in the IBA Guidelines, it seems inescapable that an arbitrator might have a potential conflict of interest as a result of portfolio financing. For example, if an arbitrator provided consultative advice to the funder in selecting a particular case, serving as an arbitrator in that case would seem to raise a conflict of interest for the arbitrator whether that case was funded as part of a portfolio or funded as an

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156 For a description of “portfolio funding” or “law firm financing,” see Chapter 2, p. 28.
individual case. The same might be true if the arbitrator sat on the Board of Directors of that funder, or had been re-appointed in numerous cases in the same portfolio of funded cases.157

As portfolio financing, and other forms of third-party funding, were not well known when the IBA undertook its 2014 revisions, the drafters were likely unable to fully consider the implications of their relatively narrow definition. The Task Force anticipates that with any future revisions to the Guidelines, the IBA may reconsider its definition. In the meantime, the Task Force’s broader definition can be used for determining the scope of disclosures, which may then be analyzed under existing IBA Guidelines.

B. The Task Force Definition

The disclosure recommendations of this Chapter are applicable to funders who fall within the following definition:

For the purposes of assessing potential conflicts of interest, the terms ‘third-party funder’ and ‘insurer’ refer to any natural or legal person who is not a party to the dispute but who enters into an agreement either with a disputing party, an affiliate of that party, or a law firm representing that party, in order to finance part or all of the cost of the proceedings, either individually or as part of a selected range of cases, and such financing is provided either through a donation or grant, or in return for remuneration dependent on the outcome of the dispute.

This definition is intended to be broad, but also does not apply to certain types of funding for which alternative rules regarding disclosure and conflicts of interest exist, as discussed below.

i. Scope of Definition

This definition applies not only to traditional claimant-side funding, in which funding is provided in expectation of a return on investment, but also to defense-side funding and pro-bono representation. For example, in the investment arbitration case brought by Philip Morris against Uruguay, The Bloomberg Foundation and its “Campaign for Tobacco-Free Kids” provided outside financial support for the Uruguayan government.158

157 See Victoria Shannon SAHANI, “Reshaping Third-Party Funding”, 91 Tulane L. Rev (2017) p. 405 (analysing in detail the conflicts of interest that may arise if the funder combines with a party or if the funder combines with a law firm).

158 See Press Release by Uruguay’s Counsel, Foley HOAG LLP, “Government of Uruguay Taps Foley Hoag for Representation in International Arbitration Brought by Philip Morris to Overturn Country’s Tobacco Regulations”
This definition is also intended to apply not only to individually funded cases, in which a funder’s support is directed specifically at individual cases, but also to other models of funding, in which the investment is in a portfolio of cases represented by a particular law firm.

There was considerable debate on the Task Force about whether this definition should include insurers, including liability insurers, after-the-event, and before-the-event insurers. On the one hand, liability insurers have interests in and, depending on the type of insurance and the jurisdiction, may exercise control over key aspects of a party’s case that are largely similar to the kinds of control exercised by modern third-party funders. For some on the Task Force, these similarities raised questions of fairness in treating similarly situated entities in similar manner for the purposes of disclosure. [Principle 2, Alternative A].

On the other hand, it was noted that various forms of insurance are ubiquitous in international arbitration, have existed for many years, and have not historically been considered subject to assessment with respect to potential arbitrator conflicts. For some, the exclusion of insurers from conflicts of interest assessment was an historical anomaly that should be corrected in conjunction with taking up the issue of third-party funding since insurers may be considered to be a form of funding by a third-party. Meanwhile, others expressed the view that exclusion of insurers was a structural feature of dispute settlement that should not be tampered with and could be maintained as separate from the issue of third-party funding. Under this view, [Principle 2, Alternative B], disclosure and conflicts of interest with respect to insurers should not be considered, much less recommended, in the absence of special consideration of the special market and regulatory issues that prevail in the insurance industry.

On the merits, some types of relationships with insurers would raise obvious conflicts. For example, an arbitrator may serve on a Board of Directors of an insurance company or hold significant stock in an insurance company that held as one of its major assets a sizable policy indemnifying a party. An arbitrator’s law firm might have an insurance company as a client, or may have an agreement by which it is retained to represent the company’s insureds. These examples undeniably raise potential conflicts that should be disclosed.

Similarly, it would be difficult to articulate a rationale for why a conflict may exist if a third-party funder was involved in multiple cases in which the same arbitrator was appointed, but the same activity by an insurer would not similarly constitute a conflict. For these reasons, most Members of the Task Force were of the view, consistent with the IBA Guidelines that the definition of third-party funding in this Chapter should extend to insurance (outside of maritime arbitration). One member of the Task Force disagreed with this view, and the notion that insurers can necessarily raise similar potential conflicts of interest as other types of funders.


159 See Chapter 2, at p. 24.
Unlike the IBA definition, the definition adopted in this Chapter clearly extends to portfolio funding and law firm financing. Specifically, it applies when funds are extended to finance an arbitration “either individually or as part of a selected range of cases.” The definition adopted also avoids the ambiguity in the IBA Guidelines’ definition between direct and indirect economic interests by referring to funding that is provided “in return for remuneration dependent on the outcome of the dispute.” Thus, the definition would apply to law firm portfolio financing models in which a funder finances one portfolio of cases (portfolio A), but the funders’ returns are linked only to the outcomes in portfolio B, which may be a subset of portfolio A.

ii. Exclusions from Definition

The definition in this Chapter is broad, but it does not extend to certain types of dispute financing that are required to be disclosed by other rules. For example, for some purposes, contingency fee arrangements or conditional fee arrangements may also be within the definition of third-party funding. However, separate rules exist that require disclosure of lawyers and law firms involved in international arbitration. Based on these existing disclosure requirements, arbitrators already consider the potential for conflicts of interest with lawyers and law firms, and that analysis would not change if the law firm were providing representation on a contingent or conditional fee basis.

The definition in this Chapter also does not necessarily extend to certain types of funding that are structured as equity investments that are being reported in some investment arbitration cases, or debt instruments, for example a loan provided by a parent company. For dispute funding that is facilitated through equity and debt-based arrangements, disclosure may be required for other reasons.

For example, General Standard 7(a) of the IBA Guidelines provides that disclosure for the purpose of assessing conflicts applies not only to a party, but also to “another company of the same group of companies [as the party], or an individual having a controlling influence on the party in the arbitration.” A funder that acquires sufficient shareholdings to influence decisions about how to manage the dispute would qualify as having a “controlling influence,” and should therefore be disclosed. In addition, the individual IBA Guidelines also apply not only to parties, but also to

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160 See Chapter 2, p.15.
“affiliates” of the parties. A related company that provides funding, for example through intercorporate loans, would be disclosable under this requirement.

Unfortunately, these provisions in the IBA Guidelines could be more clear and precise. For example, greater specificity would be useful for determining when an influence is “controlling,” or how “group of companies” is defined. Future revisions to the IBA Guidelines may address these issues, for example, by specifying specific percentage holdings, such as provided in some domestic procedural and disclosure rules.

In addition, as explained in Chapter 1 (Introduction) and Chapter 2 (Definitions), the recommendations of this Report do not extend to maritime arbitration. It was recognized that funding provided through Shipowners’ and Defence Clubs are similar to modern third-party funding, and hence raises some of the same concerns about potential arbitrator conflicts of interest. The Task Force did not study the existing practices in maritime arbitration, however, and, therefore, as noted in Chapter One, expressly excludes maritime arbitration from any recommendations in this Report.

Finally, although the Task Force concluded that the presence and identity of a funder should be disclosed or disclosable to permit arbitrators to assess conflicts of interest, the potential for arbitrator conflicts should generally not be considered a basis for requiring disclosure of any additional details about the funding relationship or funding agreement. Such details are generally irrelevant to questions of arbitrator conflicts of interest.

This recommendation is made, however, in recognition that the need for transparency and avoidance of conflicts must be counterbalanced by meaningful responses by opposing parties to exploit the participation of a funder to gain an unfair strategic advantage. Tribunals should remain mindful of potential dilatory requests or arguments to the tribunal based on unfounded assertions about the consequences of a funder’s participation.

iii. Standards for Disclosure


163 For example, Rule 29.6 of the Rules of Court of the U.S. Supreme Court requires disclosure of an ownership interest only when it exceeds 10%.

164 See Chapter 2 (Overview of Funding Market); Chapter 3 (Definitions).

165 Ibid.

166 Ibid.
There is general agreement that disclosure of the identity of a funder is necessary for an arbitrator to undertake analysis of potential conflicts of interest. There is less consensus about how and when such disclosure should occur.

Some sources that have attempted to address the issue of disclosure and potential conflicts of interests nevertheless do not address precisely when and how disclosure about a third-party funder should be made. Nevertheless, these sources generally all suggest that potential conflicts of interest arising from the involvement of third-party funders should be considered by arbitrators.

a. Guidance from Institutions

As examined in detail above, the first entity to promulgate guidelines regarding third-party funding was the International Bar Association (IBA) in its Guidelines on Conflicts of Interest in International Arbitration, last revised in 2014. Since that time, only a few institutions have specifically addressed the issue. Of those that have, none appear to require expressly the systematic disclosure of third-party funding as a matter of course, but instead leave the issue to the discretion of arbitrators.

In December 2015, the ICC Commission on Arbitration issued a Report entitled “Decisions on Costs in International Arbitration” that provided some guidance to arbitrators regarding third-party funding. Notably, the Commission provides a different definition of a third-party funder in Footnote 44 of its report:

“A third-party funder is an independent party that provides some or all of the funding for the costs of a party to the proceedings (usually the claimant), most commonly in return for an uplift or success fee if successful.”

The Report does not suggest that the existence and identity of the funder must be disclosed as a matter of course, but instead provides as follows:

“The tribunal might also consider discussing with the parties, at the outset of the arbitration or during the proceedings (typically at the first case management meeting), other aspects of cost management, including… sensitive matters, such as whether there is third-party funding and …whether the identity of the third-party funder (which could be relevant to possible conflicts of interest) should be disclosed.”

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The report also provides a worldwide survey of laws regarding disclosure of third-party funding (beginning on page 45) and a worldwide survey of cost provisions in all international arbitration rules (beginning on page 49).

SIAC’s newly released Investment Arbitration Rules (IARs) specifically authorize arbitral tribunals to order disclosure of the existence of third-party funding and/or the identity of such funder (IAR 24(l)) and to take account of third-party funding when apportioning costs (IAR 33.1). This complements Singapore’s legislative amendment (discussed below) to its Civil Law Act to allow for third-party funding.

The ICC Court of Arbitration adopted a definition of third-party funding that appears to more closely resemble the IBA Guidelines than the ICC Commission’s Report. In its Note to parties and arbitral tribunals on the conduct of the arbitration under the ICC Rules of Arbitration (22 Sep 2016 version), the ICC Court gives arbitrators the following guidance in Paragraph 24:

“Relationships between arbitrators, as well as relationships with any entity having a direct economic interest in the dispute or an obligation to indemnify a party for the award, should also be considered in the circumstances of each case.”

This instruction for arbitrators to consider relationships with third-party funders would seem to imply arbitrators have a duty to investigate the existence of a funder in an arbitration.

b. National Legislation

Few jurisdictions have specifically sought to regulate disclosure of third-party funding in international arbitration. The two exceptions are Hong Kong and Singapore, which recently enacted reforms to remove prohibitions that were regarded as previously prohibiting such funding in locally seated arbitrations. Notably, both these reforms mandate disclosure of the existence of funding and identity of the funder.

With respect to statutes, Singapore has recently introduced new legislation that allows third-party funding in international arbitration. Amendments to the Legal Profession...
(Professional Conduct) Rules 2015 require that a legal practitioner must disclose “to the court or tribunal, and to every other party to those proceedings” along with “the identity and address of any third-party funder involved in funding the costs of those proceedings.” Disclosure must be made “at the date of commencement of the dispute resolution proceedings where the third-party funding contract is entered into before the date of commencement of those proceedings” or “as soon as practicable” after the third-party funding contract is entered into.

Hong Kong has adopted legislation that is similar to that of Singapore with respect to its requirements for disclosure of third-party funding in international arbitration. Under the new Hong Kong law, a funded party must disclose “the fact that a funding agreement has been made” and the “name of the third party funder.” Notice of the funding agreement must be given “before the commencement of the arbitration” or for a funding agreement made after commencement of the arbitration “within 15 days after” the funding agreement is made. Notice must be given to “each other party to the arbitration” and to the “arbitration body.” Similarly, a funded party must give notice to the other party and the arbitration body of the termination of a funding agreement within 15 days after the funding agreement ends.

c. Trade and Investment Treaties

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174 Ibid at §49(A)(1)(a)
175 Ibid at §49(A)(1)(b)
176 Ibid at §49(A)(2)(a)
177 Ibid at §49(A)(2)(b)
180 Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Bill 2016 at §98T (1)(a)-(b).
181 Ibid at §98T (2)(a)-(b)
182 Ibid at §98T (3)(a)-(b)
183 Ibid at §98U (1)-(3).
A few trade and investment treaties, and some proposed treaty provisions, have also recently sought to introduce disclosure obligations with respect to third-party funding. These instruments expressly require disclosure of funding arrangements.

The Comprehensive Economic and Trade Agreement (CETA), recently ratified by Canada and the European Union, contains the following provisions relating to third-party funding:

“Article 8.1: Definitions
third-party funding means any funding provided by a natural or legal person who is not a disputing party but who enters into an agreement with a disputing party in order to finance part or all of the cost of the proceedings either through a donation or grant, or in return for remuneration dependent on the outcome of the dispute.

Article 8.26: Third party funding
1. Where there is third party funding, the disputing party benefiting from it shall disclose to the other disputing party and to the Tribunal the name and address of the third party funder.
2. The disclosure shall be made at the time of the submission of a claim, or, if the financing agreement is concluded or the donation or grant is made after the submission of a claim, without delay as soon as the agreement is concluded or the donation or grant is made.”

The EU has proposed including provisions regarding third-party funding in the Transatlantic Trade and Investment Partnership, negotiation of which is on hold at the time of writing. The EU’s proposed language is as follows:

“Article 1, Scope and Definitions:
2. For the purposes of this Section: ‘Third Party funding’ means any funding provided by a natural or legal person who is not a party to the dispute but who enters into an agreement with a disputing party in order to finance part or all of the cost of the proceedings in return for a remuneration dependent on the outcome of the dispute or in the form of a donation or grant.

Article 8, Third party funding
1. Where there is a third party funding, the disputing party benefiting from it shall notify to the other disputing party and to the Tribunal, or where the division of the

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Tribunal is not established, to the President of the Tribunal, the name and address of the third party funder.

2. Such notification shall be made at the time of submission of a claim, or, where the financing agreement is concluded or the donation or grant is made after the submission of a claim, without delay as soon as the agreement is concluded or the donation or grant is made.”

Some draft or model Bilateral Investment Treaties apparently include similar disclosure obligations. As of the date of publication of this Report, those drafts were not publicly available.

Several international investment arbitration cases, as well as a few international commercial arbitration cases and domestic court cases, have addressed the issue of disclosure of third-party funding.

Apparently the first, and most controversial, investment arbitration involving disclosure of third-party funding was *RSM Production Corporation v Saint Lucia*, where disclosure was sought in relation to costs, not in relation to potential conflicts of interest. It resulted, however, in a challenge to one arbitrator as a result of strong language used to describe regarding third-party funding in an Assenting Opinion. The claimant’s principal grounds for the challenge were as follows:

“The description of third-party funders as ‘mercantile adventurers’ and the association with ‘gambling’ and the ‘gambler’s Nirvana: Heads I win and Tails I do not lose’ are, in Claimant’s view, radical in tone and negative and prejudge the question whether a funded claimant will comply with a costs award. Additionally, Claimant derives from [the arbitrator’s] determinations that his alleged bias against the funders extends to Claimant as the funded party as well. Claimant contends that the language used by [the arbitrator] cannot be qualified as a neutral discussion of the issues or a mere rhetorical emphasis.”

The other two arbitrators rejected the challenge and articulated the following reasoning:

“The expressions used by [the challenged arbitrator] in his Assenting Reasons, such as ‘gambling,’ ‘adventurers’ and the reference to the ‘gambler’s Nirvana’ are strong and figurative metaphors. However, in our view, these expressions primarily serve the purpose

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186 See *RSM Production Corporation v Saint Lucia*, (ICSID Case No ARB/12/10), Decision on claimant’s proposal for the disqualification of Dr Gavan Griffith QC, IIC 662, (23 October 2014).
187 See *RSM Production Corporation v Saint Lucia*, (ICSID Case No ARB/12/10), Decision on claimant’s proposal for the disqualification of Dr Gavan Griffith QC, IIC 662, (23 October 2014) para. 42.
of clarifying and emphasizing the point [the challenged arbitrator] purports to make, namely the paramount importance, in his opinion, of third-party funding of a party in connection with a request for security for costs. We do not regard it to be established that these terms reveal any underlying bias against third-party funders in general or Claimant in particular. The means of expressing a point of view or articulating an argument may vary from one arbitrator to another, and different arbitrators possess varied characteristics, including their habits of drafting decisions and the wording used. As long as such wording does not clearly reveal any preference for either party, it cannot serve as a ground for a challenge.…. As we require an objective standard to be met, Claimant needs to establish facts indicating [the challenged arbitrator]’s lack of impartiality. However, in this case, the facts presented are that [the challenged arbitrator] issued his Assenting Reasons with the contents as described by Claimant. These facts, however, are as such not sufficient to constitute a lack of impartiality. The underlying arguments, as presented by [the challenged arbitrator] and the wording, in our view, do not cast reasonable doubt upon [the challenged arbitrator]’s capacity to issue an independent and impartial judgment in the present arbitration.”

This case has been the subject of substantial discussion, in large part because of the strong language in the assenting opinion and the subsequent challenge to its author, as well as subsequent efforts to annul the award on the merits.

In most cases when disclosure has been ordered, the arbitral tribunal orders disclosure of the identity of the third-party funder, but only rarely disclosure of the terms of the funding arrangement, and usually not for reasons related to arbitrator conflicts. For example, a dispute regarding termination of the funding arrangement in the ICSID case S&T Oil Equipment & Machinery Ltd v Romania was litigated in the U.S. courts, which required disclosure of the terms of the funding arrangement in dispute. As a result of this dispute over the funding arrangement, the funder, Juridica, ceased paying the S&T Oil’s fees and costs in the ICSID case, and the ICSID tribunal ultimately terminated the proceedings due to this non-payment. In this case, the funding agreement was in dispute, so disclosure of its terms was appropriate.

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188 See RSM Production Corporation v Saint Lucia, (ICSID Case No ARB/12/10), Decision on claimant’s proposal for the disqualification of Dr Gavan Griffith QC, IIC 662 (2014), (23 October 2014), paras. 87, 90.
In most cases, however, the funding agreement is not in dispute, so disclosure of its terms is not appropriate for the purposes of assessing potential conflicts of interest. For example, in the ICSID case *EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic*, the tribunal ordered the claimant to reveal the identity of its third-party funder for the purposes of checking for arbitrator conflicts of interest, but did not require the claimant to disclose any of the terms of the funding arrangement. In that case, the claimant had previously voluntarily disclosed that it was funded by a Luxembourg-based funder, but the claimant did not disclose the identity of that funder until ordered to do so by the tribunal.

*Muhammet Çap & Sehil Inşaat Endustri ve Ticaret Ltd Sti v Turkmenistan*, an ICSID case, provides an example of a tribunal ordering a claimant to disclose both the identity of the funder and the terms of the funding arrangement. In doing so, the tribunal invoked its “inherent powers to make orders of the nature requested where necessary to preserve the rights of the parties and the integrity of the process.” In April 2014, Turkmenistan had requested the tribunal to order the claimant to disclose whether it had engaged the services of a third-party funder as well as the terms of that arrangement. In Procedural Order No. 2, the tribunal refused the request and listed several reasons why a tribunal could justifiably order disclosure of third-party funding.

“It seems to the Tribunal that the following factors may be relevant to justify an order for disclosure, and also depending upon the circumstances of the case:

a. To avoid a conflict of interest for the arbitrator as a result of the third party funder;

b. For transparency and to identify the true party to the case;

c. For the Tribunal to fairly decide how costs should be allocated at the end of any arbitration;

d. If there is an application for security for costs if requested; and

e. To ensure that confidential information which may come out during the arbitral proceedings is not disclosed to parties with ulterior motives.”

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191 *See* *EuroGas Inc and Belmont Resources Inc v Slovak Republic*, (ICSID Case No ARB/14/14), *Transcript of the First Session and Hearing on Provisional Measures* (17 March 2015), p. 145 (“We think that the Claimants should disclose the identity of the third-party funder, and that third-party funder will have the normal obligations of confidentiality.”).

192 *See* *Muhammet Çap & Sehil Inşaat Endustri ve Ticaret Ltd Sti v Turkmenistan*, (ICSID Case No ARB/12/6), Procedural Order No 3 (12 June 2015).


194 *Muhammet Cap & Sehil Insaat Endustri ve Ticaret Ltd. Sti. v. Turkmenistan*, (ICSID Case No. ARB/12/6), Decision on Jurisdiction, (13 February 2015), para. 50 (quoting Procedural Order No. 2).
One year later, Turkmenistan renewed its request for such disclosure to ensure that there were no conflicts of interests with the arbitrators or counsel in the case and to check whether the claimants were “still the actual owners of the claims in this arbitration.”\textsuperscript{195} To bolster its renewed request, Turkmenistan also cited the newly enacted General Standard 7(a) and the Explanation to General Standard 7(a) of the International Bar Association (IBA) Guidelines on Conflicts of Interest in International Arbitration, which took effect in October 2014.\textsuperscript{196} Turkmenistan also stated that it was considering applying for security for costs in the case due to the presence of the third-party funder.\textsuperscript{197} In Procedural Order No. 3, the tribunal decided to grant Turkmenistan’s renewed request for the following reasons:

“First, the importance of ensuring the integrity of the proceedings and to determine whether any of the arbitrators are affected by the existence of a third-party funder. In this respect the Tribunal considers that transparency as to the existence of a third-party funder is important in cases like this. Second, although it has not yet done so, Respondent has indicated that it will be making an application for security for costs. It is unclear on what basis such application will be made, e.g. Claimants’ inability to pay Respondent’s costs and/or the existence of a third-party funder. There are two additional factors which the Tribunal considers support the conclusion it has reached. Claimants have not denied that there is a third-party funder for the claims in this arbitration. It would have been straightforward to do so, just as they denied having assigned any of their rights to another party. Furthermore, and this was not denied by Claimants, Respondent has alleged that the order for costs in favour of Respondent made by the Kılıç Tribunal\textsuperscript{198} has not been paid even though the claimant (Kılıç İnşaat İthalat İhracat Sanayi ve Ticaret Anonim Şirketi) has funded the annulment proceedings.”\textsuperscript{199}

It is important to note that the tribunal did not specify in its procedural order which of the terms of the funding arrangement were required to be disclosed and which could stay confidential.\textsuperscript{200} This creates uncertainty regarding whether such disclosure may unfairly disadvantage the disclosing party or unfairly advantage the party receiving the information.

Similarly, in the PCA case \textit{South American Silver v. Bolivia}, Bolivia “request[ed] the Tribunal to order the Claimant to ‘disclose the identity of the funder of this arbitration, as well as

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\textsuperscript{195} \textit{See Procedural Order No. 3, supra} note 192, at para. 2.
\textsuperscript{196} \textit{Ibid.} at para. 2.
\textsuperscript{197} \textit{Ibid.} at para. 2.
\textsuperscript{198} \textit{Kılıç İnşaat İthalat İhracat Sanayi ve Ticaret Anonim Şirketi v Turkmenistan}, (ICSID Case No ARB/10/1) Award (3 July 2013).
\textsuperscript{199} \textit{Ibid.} at paras. 9-12.
\end{flushright}
the terms of the funding agreement signed with him.™  Like in the Muhammet Cap case, it
would appear that the parent company of the claimant had earlier voluntarily disclosed
the existence of the third-party funding, but not the identity of the funder or the terms of the
agreement.192 Like Turkmenistan, Bolivia argued that it was seeking this disclosure and security
for costs due to the economic difficulties of the claimant coupled with the existence of third-party
funding.193 Bolivia also cited the 2014 IBA Guidelines provision “that third-party funders should
be equated with the funded party to verify the existence of conflict of interests, and that the funded
party is obliged to disclose any relationship that exists between her (including third-party funders)
and the arbitrators.”194

In its reply to Bolivia’s request, South American Silver (SAS) agreed to disclose the name
of its funder but noted that “the terms of SAS’s funding agreement are irrelevant to the issues in
dispute in this arbitration and that the terms of that agreement are confidential, commercially
sensitive, and that SAS and the funder would incur prejudice if the Tribunal ordered SAS to
disclose the terms of the funding agreement.”195 With respect to Bolivia’s application for security
for costs, the tribunal adopted the standard articulated by the majority of the tribunal in RSM v.
Saint Lucia and EuroGas v. Slovak Republic that “the mere existence of a third-party funder is not
an exceptional situation justifying security for costs.”196 In the end, the tribunal decided to order
disclosure of the name of the funder “for purposes of transparency, and given the position of the
Parties” but determined that there was no basis to order disclosure of the terms of the funding
arrangement.197

The foregoing cases have all addressed cases involving for-profit third-party funding. There is another category of funders which may be termed “not-for-profit funders.”198 These funders are motivated to bring about a certain outcome in the case or a change in the law, rather than motivated by making a profit. The most widely known example of a “not-for-profit” funding arrangement is the arrangement whereby the Bloomberg Foundation and its “Campaign for Tobacco-Free Kids” donated $200,000 to Uruguay to help it fight against Philip Morris in the

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202 Ibid. at para. 25.
203 Ibid. at para 25.
204 Ibid. at para. 29.
Opposition to Respondent Request for Cautio Judicatum Solvi and Disclosure of Information, (14 December 2015)
paras. 38, 40.
206 Ibid. at para. 74 (citing EuroGas Inc. & Belmont Resources Inc. v. Slovak Republic, (ICSID Case No.
ARB/14/14) Procedural Order No. 3 – Decision on Requests for Provisional Measures, (23 June 2015) para. 123.
207 Ibid. at paras. 79, 80, 84.
208 See e.g., Eric DE BRABANDERE and Julia LEPELTAK, “Third-Party Funding in International
ICSID case *Philip Morris v. Uruguay* in which Philip Morris challenged state regulations requiring plain packaging of tobacco products.\(^{209}\)

Bloomberg did not expect any monetary reimbursement of its investment or have any economic interest in the award. Instead it was seeking to bring about a certain outcome in the case, namely to allowing Uruguay to successfully defend a suit challenging its laws regarding tobacco packaging.

It remains uncertain the extent to which not-for-profit funding will continue to grow. Particularly in investment arbitration, where awards are routinely relied on as a form of soft precedent, it may become more common for States that are not a party in a particular case, or non-profit entities, to support responding parties in order to affect development of the law or to protect their own rights indirectly.\(^{210}\) To date, it would appear that many not-for-profit funders and the parties they fund are inclined to voluntarily, and even publicly, announce their involvement in the case, perhaps to sway public opinion in their favour or to attract additional funding sources for the funded party.\(^{211}\)

4. **When Disclosure Should be Made and By Whom**

A general principle that the presence and identity of funders should be disclosed raises separate questions about who bears the burden of such disclosure, to whom such disclosure should be made, and under what conditions.

Because third-party funders are not, by definition, usually parties to the arbitration, they cannot be directly compelled by an arbitral tribunal or rules applicable within the arbitral proceedings to disclose their participation. Instead, disclosure is ordinarily effectuated through the parties.

This obligation is delineated in IBA General Standard 7(a), which requires parties to inform arbitrators, as follows:

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\(^{209}\) See *Philip Morris Brand Sàrl (Switzerland), Philip Morris Products SA (Switzerland) and Abal Hermanos SA (Uruguay) v Oriental Republic of Uruguay*, (ICSID Case No ARB/10/7).

\(^{210}\) For example, Global Petroleum Group funded both Grenada and St Lucia in their efforts to defend against competing claims for access to oil reserves asserted by rival RSM. It has been alleged that Global Petroleum Group had obtained its right to access oil reserves based on “corrupt ties to the government of Grenada.” See Fernando CABRERA DIAZ, *RSM Production Corp. files second arbitration against Grenada, sues Freshfields*, [https://www.iisd.org/itn/2010/04/08/rsm-production-corp-files-second-arbitration-against-grenada-sues-freshfields/](https://www.iisd.org/itn/2010/04/08/rsm-production-corp-files-second-arbitration-against-grenada-sues-freshfields/), last accessed 30 August 2017.

“A party shall inform an arbitrator, the Arbitral Tribunal, the other parties and the arbitration institution or other appointing authority (if any) of any relationship, direct or indirect, between the arbitrator and the party (or another company of the same group of companies, or an individual having a controlling influence on the party in the arbitration), or between the arbitrator and any person or entity with a direct economic interest in, or a duty to indemnify a party for, the award to be rendered in the arbitration.”

At the end of General Standard 7(b), the provision clearly states that “The party shall [make required disclosures] on its own initiative at the earliest opportunity.” In addition, General Standard 7(c) further states “In order to comply with General Standard 7(a), a party shall perform reasonable enquiries and provide any relevant information available to it.”

Members of the Task Force disagreed about what relationships are required to be disclosed under General Standard 7, and how the reporting obligations in General Standard 7 relate to arbitrators’ disclosure obligations under General Standard 6. Some members interpreted General Standard 7 as requiring only that parties disclose to arbitrators information that would constitute a disclosable “relationship” under General Standard 6 or the individual Guidelines in the Red and Orange lists. Under this view, the presence and identity of a funder (or insurer) would only need to be disclosed in certain circumstances, namely if a funder might have a material relationship with an arbitrator that might give rise to a potential conflict of interest. A funder who had never had any contact or interaction with an arbitrator, or that has not funded numerous cases involving that arbitrator, would, according to this view, not need to have its presence and identity in the case disclosed.

Others on the Task Force disagreed with this interpretation. Their concern was that, as a practical matter, this narrower interpretation would effectively shift both the substance of the disclosure obligation and discretion in interpreting the IBA Guidelines not to parties, but to funders. For example, parties know whether their current case is funded, but they do not and cannot know of every relevant contact or relationship that may exist as between a funder and an arbitrator. For example, unbeknownst to a party, its funder many have funded several cases in the past few years in which the same arbitrator was appointed. In the absence of mandatory, systematic disclosure, the arbitrator would likewise be unaware and unable to know of the repeated appointments.

It is plausible that a party, as part of its duty under General Standard 7(c), could make reasonable enquires of the funder about whether any such circumstances exist. However, not all of the IBA Guidelines are as straightforward as those that require the counting of cases and the counting of years, and in some instances, even those provisions involve nuanced assessments. If a party is only obliged to disclose the presence and identity of a funder when the funder has identified a relationship that is disclosable, then all the nuanced interpretation of what constitutes a disclosable relationship or a potential conflict of interest rests with the funder. The funder may
or may not be particularly well-versed in the IBA Guidelines and related standards that govern arbitrators’ conflicts of interest.

The larger problem, for those Members who objected to the narrower reading of General Standard 7, is that it is arbitrators, not parties or funders, who are obligated to determine and disclose particular facts that may give rise to a conflict of interest. This obligation to assess potential conflicts of interest also implies a duty to investigate, which in turn obliges arbitrators to make reasonable inquiries. Those on the Task Force who supported systematic disclosure at the beginning of cases relied in large part on this duty to investigate: Arbitrators’ duty to make reasonable inquiries presumably obliges them to request disclosure of the existence of funding and the identity of the funder in every case since, absent such disclosure, they may have conflicts that are not known.

5. Unknown Conflicts of Interest

One argument considered but ultimately rejected by the Task Force is that relationships with funders need not be disclosed to arbitrators because unknown conflicts are not generally a basis for disqualifying arbitrators or successfully challenging an award. Unlike parties and law firms, third-party funders are not readily identifiable from the pleadings. In the absence of disclosure, this argument goes, the participation of a funder would remain unknown and unknowable and an arbitrator cannot be biased by unknown information.

This view was ultimately rejected by the Task Force, and by the standards for disclosure identified above. Study of a particular example is helpful to illustrate the point.

Third-party funders can raise potentially serious conflicts that are distinct from those that arise with either law firms or parties. For example, take the case of one party \((P1)\) that is funded by funder \((F)\) and \(X\) is the presiding arbitrator in one arbitral dispute \((A1)\), but \(X\)’s partner also serves as counsel to a claimant in another unrelated second arbitration \((A2)\) and the claim is funded by the same funder \(F\). The fact that the fees of \(X\)’s partner in \(A2\) are paid by \(F\) and that \(X\)’s partner is likely to have significant contacts with \(F\) on the basis of the funding agreement raises concerns beyond simple repeat appointments. The financial arrangement and ongoing contacts arguably raise questions about \(X\)’s impartiality and independence with respect to the claimant in \(A1\) that would make it inappropriate for \(X\) to sit as an arbitrator in \(A1\).

\[\text{Footnote 212: This hypothetical and analysis was developed by Maxi Scherer in Maxi SCHERER, “Out in the open? Third-party funding in arbitration”, CDR News (26 July 2012) available at <http://www.cdr-news.com/categories/expert-views/out-in-the-open-third-party-funding-in-arbitration> (last accessed 3 August 2017).}\]
The resolution to the problem illustrated in this example is self-evident, and generally should preclude the funder from taking on the case. If a funder were somehow to undertake such funding X would not be aware of the conflict because X would not know of the existence of a funding agreement. Absent an obligation to disclose the presence and identity of a funder, the funder’s participation in an international arbitration case is otherwise usually unknown or unknowable. The nature of funders’ relationships with attorneys and funded parties is generally unknown.

Even if unknown at the initial stages, the existence of the funding agreement may be discovered later. A number of circumstances create the possibility of disclosure: if a dispute arises between the client or the law firm and the funder; if financing is suspended or funding caps are reached that require explanations from a party about their financial situation; or if the need arises to respond to a challenge by an opposing party that a claim of financial distress is unfounded because of a suspected funding arrangement. Disclosure can also be accidental. For example, Jonas von Goeler reports, “[i]n the ICC case X v. Y and Z, for example, the claimant transferred a litigation funding agreement to the respondents without further explanation, leading counsel for the respondents to the assumption that ‘[t]his agreement was sent maybe by mistake.’” Any of these scenarios can lead to disclosure about the presence of a funder.

In addition, as Jonas Von Goeler summarizes, rules governing publicly traded companies may also oblige disclosures: “Importantly, the presence of a third-party funder may need to be disclosed for reasons not linked to the arbitration proceedings, namely to comply with public disclosure requirements imposed upon listed companies, and following disputes between the parties to the funding agreement ending up in state courts.”

Later discovery of a third-party funder whose links with an arbitrator should have been disclosed may require that the arbitrator step down or risk rendering an award that may be set aside or refused recognition and enforcement as a result of the conflict. Even if discovered after the close of proceedings, a conflict that should have been disclosed can still be a potential ground for attacking an award, even if the arbitrator was ostensibly unaware of the funding arrangement.

217 There is some disagreement among arbitrators and courts about the effect of an arbitrator’s lack of knowledge of a conflict. As the Reporters’ notes to the Restatement explain with regard to US Law:

There is some disagreement among courts about whether an arbitrator’s lack of knowledge of a conflict precludes a finding of evident partiality. Some courts have taken the view that an absence of
Eventually, it might not be proven that the arbitrator knew about the participation of the funder, and the conflict be treated therefore as an “unknown conflict.” An absence of specific knowledge about a particular conflict is not, however, universally recognized as negating allegations of bias. Particularly when circumstances create inappropriate financial relationships from which an arbitrator benefitted, challenges to an award may be effective, even if the alleged financial relationship was unknown.

Another, final reason for rejecting arguments based on unknown conflicts is that arbitrators are generally understood as having a “duty to investigate” or to take reasonable steps to inform themselves of potential conflicts of interest. For example, in General Standard 7(d), the IBA Guidelines provide (d): “An arbitrator is under a duty to make reasonable enquiries to identify any conflict of interest, as well as any facts or circumstances that may reasonably give rise to doubts as to his or her impartiality or independence. Failure to disclose a conflict is not excused by lack of knowledge, if the arbitrator does not perform such reasonable enquiries.”

Some on the Task Force view an inquiry by an arbitrator about the existence and identity of funding as part of an arbitrator’s fulfilment of this duty. Indeed, it would be difficult to argue that asking parties about whether they are funded does not fall within the duty to “make reasonable enquiries.” Under the IBA Guidelines, a failure to make a reasonable enquiry would mean that a failure to disclose is not “excused.” Under other authorities, an arbitrator’s failure to investigate a potential conflict may also be a factor to be considered in assessing the consequences of an undisclosed, unknown conflict of interest.

As a practical matter, in an effort to protect their reputations and ensure effective handling of the dispute, most arbitrators do undertake to investigate unknown potential conflicts of interest. A request that parties disclose the existence and identify of a funder would normally be a part of that effort.

Knowledge about a conflict per se precludes a finding of evident partiality. See Gianelli Money Purchase Plan & Trust v ADM Inv. Servs., Inc., 146 F.3d 1309, 1313 (11th Cir. 1998); see also Rev. Unif. Arb. Act § 12(e), 7 U.L.A. 43 (2005) (“An arbitrator appointed as a neutral arbitrator who does not disclose a known, direct, and material interest in the outcome of the arbitration proceeding or a known, existing, and substantial relationship with a party is presumed to act with evident partiality under Section 23(a)(2).”). This approach—categorically excluding from consideration all conflicts regarding which an arbitrator has no actual knowledge—arguably discourages arbitrators from fulfilling their duty to investigate. It also imposes on the aggrieved party the unreasonable burden of having to prove actual knowledge about a conflict on the part of an arbitrator. The better view, and the one represented in the final factor of the test stated in the section, is that absence of knowledge is relevant to a court’s analysis of the facts of a case, particularly as relates to the investigation undertaken by the arbitrator. See New Regency Prods., Inc. v Nippon Herald Films, Inc., 501 F.3d 1101, 1107–8 (9th Cir. 2007). If the arbitrator has taken reasonable measures to investigate potential conflicts, a lack of knowledge about a particular conflict will generally weigh significantly against a finding of evident partiality.


218 IBA Guidelines on Conflicts of Interest.

It is for these reasons that most standards that have emerged or have been adopted require general and systematic disclosure of the presence and identity of a funder but do not require disclosing the terms of the funding arrangement. This systematic but narrow disclosure regarding funders in turn allows arbitrators, whose ultimate duty it is to disclose potential conflicts, to engage in a thorough assessment of potential conflicts and make any necessary disclosures.
Chapter 5
Privilege

PRINCIPLES

1. Generally, the existence of funding and the identity of a third-party funder is not privileged information.

2. Generally, the specific provisions of a funding agreement may include privileged information, and production of it should only be ordered in exceptional circumstances.

3. For information that is determined to be privileged under applicable laws or rules, tribunals should not treat that privilege as waived solely because it was provided by parties or their counsel to a third-party funder for the purpose of obtaining funding or supporting the funding relationship.

4. If the funding agreement or information provided to a third-party funder is deemed to be disclosable, the tribunal should generally permit appropriate redaction and limit the purposes for which such information may be used.

ANALYSIS

Obtaining third-party funding and the maintenance of a funding relationship generally requires disclosure of information that would otherwise be privileged, either because it involves communications between a client and its counsel, or analysis by a client’s counsel in preparation for legal proceedings. However, when confidential or privileged information is shared with a third party, confidentiality and privilege are generally deemed waived. In the context of third-party funding, the tension between these two premises raises questions about whether otherwise privileged information disclosed to funders may result in a waiver of privilege. If so, that information could be susceptible to disclosure requests in the arbitration proceedings or related national court proceedings.

Related to this issue, some have expressed concern that a third-party funder, once in possession of a client’s confidential information, is not legally prohibited from using such information in another funded matter for a different client, even if that matter raises a potential conflict with the interests of the original client. Funders, in their capacity as funders, are not generally regarded as bound by professional ethical rules regarding treatment of confidential information and conflicts of interest rules in the same way lawyers are.220

Despite the importance of these issues, international Conventions, and most national arbitration law and arbitral rules are silent about issues of privilege.221 The rise of third-party

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220 In fact, many funding agreements expressly state that the funder is not providing legal services and that the agreement does not create an attorney-client relationship.

221 See Born at 2376.
funding has added new complexities to existing ambiguities about privilege in international arbitration.

An important starting point is that most national arbitration law, arbitral rules and the 2010 IBA Rules on the Taking of Evidence in International Arbitration (the IBA Evidence Rules) largely leave such issues to arbitrator discretion.\textsuperscript{222} Arbitrators enjoy broad discretion to control the proceedings before them, which includes determining when to order document production, whether any privileges apply to requested documents, and whether such privileges may have been waived.

The Principles in this Chapter are predicated on arbitrators’ broad authority over procedural issues, and the need to exercise that authority in light of conflicting national standards regarding privilege, and a general absence of clear standards that apply when otherwise privileged information is shared with third-party funders. This Chapter begins by outlining the scope of privileges [1.], analysing the treatment of privilege and waiver in international arbitration [2.], and summarizes the results of an international survey on privilege conducted by the Task Force [3.]. It then examines the laws that might apply to determine privilege [4.], and existing national heads of privilege and the rules that affect their applicable to funded parties [5].

1. **Scope of Privilege Issues**

Privileged information may be provided to a third-party funder in the following situations:

(i) during the initial due diligence phase (where funding is first requested and the third-party funder requires information in order to decide whether or not to provide financing); and

(ii) once the third-party funder has already committed to funding a party’s participation in a pending dispute and the party and/or its counsel is sharing information about developments as well as documents being submitted in those proceedings.

In addition, there are questions about whether the funding agreement itself is privileged.

In addition to information that is shared, there is a separate category of documents produced and held by the funder such as (i) the funder’s own evaluation of the case; (ii) documents relating to the negotiation of the funding agreement (the terms may give away thoughts on the strength of the case); and (iii) separate legal opinions from independent counsel on the strength of the case. Since the funder is not a party to the arbitration proceedings, it is difficult to see how the funder could be obliged to disclose these documents during the course of the arbitration. There may, however, be circumstances in which these documents are sought in the context of arbitration-related litigation or, in the United States, in an action to obtain document production under 28 U.S.C. § 1782. In such instances, important questions arise regarding their privileged status.

\textsuperscript{222} Von Goeler, p. 166.
2. Privilege in International Arbitration

Historically, according to leading international arbitration commentators, there has been “limited authority concerning the appropriate treatment of privileges,” in international arbitration, and international sources generally provide little guidance.223

As a practical matter, arbitrators often look to national rules and standards to determine the existence of a privilege, either as a category or as applied to particular documents. Many commentators are of the view that the weight of authority and the better view is that domestic privileges should apply, rather than international standards.225 The justification for this approach is that national law provides the basis for privileges in the first instance. Under this approach, the applicable national rule is determined through conflict of laws analysis.

Arbitrators also have considerable discretion in undertaking conflict of law analysis, though some consensus is emerging regarding the factors to take account of in determining applicable national law.226 In addition to traditional conflict of law factors, it is generally understood that “arbitral tribunals should do justice to the legitimate expectations of the parties.”227

These basic premises are reflected in the IBA Rules on the Taking of Evidence. Article 9(2)(b) authorises an arbitral tribunal, at the request of either party or at its own discretion, to exclude documents and other evidence that may be covered by privilege under the legal (and ethical) rules “determined by the Arbitral Tribunal to be applicable.” Meanwhile, Article 9(3) provides guidance to arbitral tribunals when considering a privilege issue under Article 9(2)(b).

Under Article 9(3)(a), a tribunal may take into account the need to protect the confidentiality of communications made in connection with and for the purpose of producing or obtaining legal advice. Article 9(3)(b) refers to similar protections for communications made in connection with settlement negotiations. Under Article 9(3)(c), arbitral tribunals are advised to consider the parties’ expectations at the time privilege is said to have arisen, and thus presumably most often the approach to privilege in the parties’ home jurisdictions.

Perhaps most notably, Article 9(3)(d) provides the considerations that an arbitral tribunal may “take into account” in determining waiver. Specifically, it provides that in ordering production of documents, an arbitral tribunal should consider “any possible waiver of any applicable legal impediment or privilege by virtue of consent, earlier disclosure, affirmative use

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225 BORN at 2383-2384.
226 BERGER, Evidentiary Privileges: Best Practice Standards Versus/and Arbitral Discretion, 22 Arb. Int’l 501, 514-15 (2006). This pragmatic consensus is based on four key observations: (1) Privilege issues must be qualified as substantive law issues. (2) The parties’ standard choice of law clause in the contract usually does not extend to the issue of evidentiary privileges. (3) In determining the law applicable to a certain privilege issue, the tribunal shall apply the law of the jurisdiction with which the relevant communication is most closely connected, i.e., the law where the party has its place of business. (4) The tribunal may exclude evidence from both sides which is privileged under the law of one party but not under the law of the other based on compelling considerations of fairness or equality.”
227 Klaus Peter BERGER, Evidentiary Privileges: Best Practice Standards vs./and Arbitral Discretion, in: Best Practices in International Arbitration (Markus Wirth, editor) (ASA Swiss Arbitration Association Special Series No. 26, July 2006).
of the Document, statement, oral communication or advice contained therein, or otherwise.” This language is limited in the precatory language of Article 9(3) with the proviso “insofar as permitted by any mandatory legal or ethical rules that are determined by it to be applicable.”

The privilege status of documents provided to third-party funders is often described as a question of whether the privilege “extends” to the funding relationship. It is more accurate, however, to frame the question of whether the sharing of documents with a third-party funder constitutes waiver. This distinction has important consequences, particularly under the framework of the IBA Rules for Evidence, for evaluating the privilege status of documents shared with a third-party funder.

Under international standards and Article 9(2)(b), the existence of a privilege is to be determined by reference to national law that the tribunal determines to be applicable. On the other hand, Article 9(d) makes determination of waiver of “any applicable … privilege” dependent on factual and prudential considerations. Reading these two provisions together, they suggest that the existence of a privilege should be made based on a conflict of laws analysis, but findings of waiver are not similarly predicated on conflict of laws analysis.

As examined in greater detail below and in the Annex, national laws differ significantly with respect to the “heads of privilege” they create, and the scope of such privileges. Most national laws do not clearly address, however, whether provision of privileged documents to a third-party funder would constitute a waiver. In light of these ambiguities, Article 9(3)(d) of the IBA Rules of Evidence becomes a compelling basis for concluding that tribunals should, as the Principles in this Chapter suggest, independently analyze whether a waiver has taken place.

In undertaking this analysis, another provision in the IBA Rules of Evidence is helpful. Apart from privileges established by national law, arbitral tribunals are separately authorized under Article 9(2)(e) to decline to order production on “grounds of commercial or technical confidentiality that the Arbitral Tribunal determines to be compelling.” Documents provided subject to the types of non-disclosure agreements typically entered into between funders and parties would seem to establish commercial confidentiality. Protection against disclosure would seem to be particularly compelling when disclosure would involve otherwise privileged documents.

In addition, other provisions in Article 9 instruct tribunals to consider more fairness-related issues. Under Article 9(3)(d), the arbitral tribunal is encouraged to consider whether a party’s rights to privilege have been waived. Under Article 9(3)(e), the arbitral tribunal is urged to maintain fairness and equality between the parties, particularly relevant where different rules of privilege apply to each party so that one party appears able to shield documents from disclosure while the other does not. This may involve applying the broadest standard of protection available to all parties to the arbitration.

While the IBA Rules of Evidence are not binding on arbitral tribunals, they are frequently a point of reference. To the extent they support the notion that the provision of privileged documents to a third party does not necessarily constitute waiver of privilege, the Task Force concluded they provide a firm basis for informing Principle 3 in this Chapter.

Institutional rules are generally less specific than the IBA Rules. The various institutional rules generally do not specify the criteria a tribunal may wish to consider when determining issues
of privilege and confidentiality. Many of the main arbitral institutions simply state in their rules that the tribunal has the final say as to the admissibility of any evidence, including whether or not to apply strict rules of evidence (which will include legal privilege). For example:

(i) **The UNCITRAL Model Law (2006):**

   “Article 19. Determination of rules of procedure

   (1) Subject to the provisions of this Law, the parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.

   (2) Failing such agreement, the arbitral tribunal may, subject to the provisions of this Law, conduct the arbitration in such manner as it considers appropriate. The power conferred upon the arbitral tribunal includes the power to determine the admissibility, relevance, materiality and weight of any evidence.”

(ii) **The UNCITRAL Rules (2010):**

   “Evidence

   Article 27

   ... 3. At any time during the arbitral proceedings the arbitral tribunal may require the parties to produce documents, exhibits or other evidence within such a period of time as the arbitral tribunal shall determine.

   4. The arbitral tribunal shall determine the admissibility, relevance, materiality and weight of the evidence offered.”

(iii) **The ICC Arbitration Rules (2017):**

   “Article 22: Conduct of the Arbitration

   2) In order to ensure effective case management, the arbitral tribunal, after consulting the parties, may adopt such procedural measures as it considers appropriate, provided that they are not contrary to any agreement of the parties.

   3) Upon the request of any party, the arbitral tribunal may make orders concerning the confidentiality of the arbitration proceedings or of any other matters in connection with the arbitration and may take measures for protecting trade secrets and confidential information.”

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(iv) **LCIA Rules (2014):**

   “Article 22 Additional Powers

   22.1 The Arbitral Tribunal shall have the power ...

   (vi) to decide whether or not to apply any strict rules of evidence (or any other rules) as to the admissibility, relevance or weight of any material tendered by a party on any issue of fact or expert opinion; and to decide the time, manner and form in which such material should be exchanged between the parties and presented to the Arbitral Tribunal...”

Accordingly, arbitral rules generally affirm that arbitrators are afforded considerable discretion in shaping and applying rules of privilege. In this respect, they provide additional support for the power of international arbitrators to follow the relevant Articles of the IBA Rules of Evidence and Principle 3, above, to conclude that sharing documents with third-party funders does not constitute waiver.

3. **Task Force Survey on National Practices**

   To assess existing practices and governing law in various jurisdictions, the Task Force collected reports on privilege from over 20 jurisdictions. The compiled results of this research will be made available at [http://www.arbitration-icca.org/projects/Third_Party_Funding.html](http://www.arbitration-icca.org/projects/Third_Party_Funding.html).

   Each report considers the following four questions:

   (i) Please describe, with brief reference to case law, legislation or legal writings, the privileges or other rules (e.g. professional secrecy) on which a party or its counsel may rely in order to resist disclosure in national court proceedings of communications between the lawyer and the client (or between lawyers) that would otherwise have to be disclosed. In each case, please identify who may claim the benefit of the privilege or other rule (e.g. the client, the lawyer).

   (ii) Please describe, with brief reference to case law, legislation or legal writings, the privileges or other rules (e.g. professional secret) on which a party or its counsel may rely in order to resist disclosure in arbitral proceedings (with their seat in your jurisdiction) of communications between the lawyer and the client (or between lawyers) that would otherwise have to be disclosed. In each case, please identify who may claim the benefit of the privilege or other rule (e.g. the client, the lawyer).

   (iii) Please describe the circumstances in which the benefit of the privilege or other rule may be lost in national court proceedings or arbitration. In particular, please describe the possible effect of disclosure to a third party of a communication that would have been privileged.

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229 Jurisdictions covered are: Australia, Brazil, China, England, Germany, Hong Kong, India, Japan, Netherlands, Portugal, Russia, Scotland, Singapore, South Korea, Spain, Sweden, Switzerland, Turkey, United States (California), Ukraine, United Arab Emirates. These reports will be made available at [http://www.arbitration-icca.org/projects/Third_Party_Funding.html](http://www.arbitration-icca.org/projects/Third_Party_Funding.html).
ordinarily have been protected from disclosure to a court or arbitral tribunal by reason of the privileges or similar rules described in questions 1 and 2.

(iv) Please identify the circumstances in which disclosure of an otherwise-protected communication to a third-party funder will result in loss of the benefit of the privilege or other rule, in national court proceedings or arbitration. Please identify any circumstances where the benefit of the privilege or other rule will continue to attach to the communication, notwithstanding the disclosure. Please make brief reference to case law, legislation or legal writings relevant to this question, if such exist. Where there is little or no authority on privilege and how it applies to third-party funders, please look instead at situations analogous to the third-party funder relationship e.g. with insurers.

The following additional questions were posed to reporters for consideration:

(i) What law applies to privilege in litigation in your jurisdiction/in arbitration with its seat in your jurisdiction?

(ii) Are documents held by the funder protected, i.e. the funder’s own evaluation of the case; separate legal opinions; negotiation of the funding agreement?

(iii) In relation to documents transferred by the lawyer/party to the funder, does the use of a confidentiality/non-disclosure/common interest agreement work to protect privilege/secrecy in your jurisdiction?

Based on this research, the Task Force concluded that in most jurisdictions, there is no clear answer as to whether documents and information provided to a funder will be definitively protected – in a nascent industry, lawyers may be able to advise by analogy but in many (indeed most) jurisdictions, there are no well-established precedents or rules (only limited and under-developed sources) dealing with the point.

The responses from the national lawyers who responded to the Task Force’s questionnaire demonstrate the need to take local advice on a case by case basis as treatment of “privileged” documents varies from jurisdiction to jurisdiction.

The main distinction in the treatment of information shared with funders appears between civil and common law systems, although many nuances exist even among jurisdictions on each side of this divide.

There can be some confidence that in common law jurisdictions where funding is allowed at all (notably it is prohibited in Ireland; recent reforms allow it for international arbitration and supporting litigation in Hong Kong and Singapore) an exchange of information with a funder will be protected, in particular where an appropriate contract is in place to manage confidentiality, limit waiver of privilege, assert a common interest and/or assert the application of an appropriate form of privilege.

However, caution must be exercised and advice taken in each case.230 There has been at least one case in the US where the discovery of documents provided to a funder has been ordered.

We are also aware of one case before the English courts in which the disclosure of funding documents was ordered.231

The approach of civil jurisdictions is based on the concept of “professional secrecy” according to which lawyers (but often not extending to in-house lawyers) are bound by professional duties and rights not to reveal confidential information, even if – for example- ordered by a court to testify. Whether those rights and duties could be extended to a funder with whom such information is shared depends on the rules in a particular jurisdiction. In certain jurisdictions there is no protection afforded to documents not in the lawyer’s possession or control. One can take some comfort, however, from the fact that a party is not generally required to “disclose” documents at the request of an opposing party in civil law systems, so there will be limited scenarios in which disclosure of otherwise confidential case documents becomes a real issue.

Parties and funders in practice (hope to) protect against problems by entering into appropriate confidentiality agreements before sharing information.

4. Applicable Laws and Rules that Determine Privilege

Privilege may be regarded as a matter of substance or procedure, but its status as either varies from jurisdiction to jurisdiction, and is often unclear.232 The existence and scope of privilege may be determined or affected by a range of sometimes overlapping domestic laws, professional ethics rules, and arbitral rules. To date, there has been in international arbitration the legal framework for determining how and

The various domestic laws that may be relevant include (i) the law of the jurisdiction where communications took place or the relevant document was created; (ii) the law of the jurisdiction where the document is physically located or held; (iii) the law of the jurisdiction where the counsel of each party is licensed and/or practises; (iv) the law of the jurisdiction where each party resides; (v) the law of the jurisdiction in which disclosure is sought; (vi) the law of the seat of the arbitration; (vii) the law governing the substance of the dispute or the law in relation to which the

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231 See e.g., Leader Technologies, Inc. v Facebook, Inc., 719 F.Supp.2d 373 (D.Del. 2010) (holding that common interest privilege did not exist between patentee and litigation financing companies and ordering disclosure of "limited technical documentation" that had been shared with litigation funder); Miller UK Ltd. v. Caterpillar, Inc., 17 F. Supp. 3d 711 (N.D. Ill. 2014) (upholding protection under the work product doctrine for documents disclosed to the funder due to a pre-existing confidentiality agreement between the client and the funder, but not upholding protection under the attorney-client privilege, because the court did not view the funder as falling within the “common interest” exception to waiver). In England, see Excalibur Ventures LLC v Texas Leystone Inc. and others [2012] EWHC 2175 (unreported).

232 In England & Wales, legal professional privilege is usually considered a substantive common law right. However there is still some ambiguity as to whether or not it is also a procedural right. In a landmark English case, Lord Scott held that “the debate [as to whether the right to legal advice privilege is a procedural right or a substantive right] is sterile. Legal advice privilege is both”, Three Rivers District Council and others v Governor and Company of the Bank of England (No 4) [2004] UKHL 48, Lord Scott at 26. See also, for example, the Australia report for a discussion of the status of privilege as a part of substantive law rather than a procedural rule. This leads to tensions where a matter has international elements and so a tribunal may have to apply conflicts of laws principles to decide which privilege laws apply. Contrast this with the position in civil law jurisdictions, such as The Netherlands, where the concepts of professional secrecy are derived from the Code on Civil Procedure and would appear to apply by virtue of the office of the professional instructed. Where a tribunal’s analysis of conflicts of laws principles is at odds with the professional’s duties and rights with regards to secrecy this may lead to difficulty.
legal advice was provided; (viii) the law governing the arbitration agreement and/or (ix) the law of the country with the “closest connection” to the events.

International arbitral tribunals may need to conduct a conflict-of-laws analysis to determine which applicable law governs the existence and scope of any claimed legal privilege. In practice tribunals often apply a “closest connection” test to avoid this complex analysis.

In addition to the rules and laws that may be formally applicable, tribunals may also take into consideration more practical considerations, such as the materiality of the documents in question, or the equality between the parties, to ensure that the same protection is afforded to documents of both parties, or in other words that the broadest standard of protection is applied to all privileged documents concerned.

The professional/ethical obligations of a lawyer will also play a part in the way information or evidence may be protected within certain jurisdictions, particularly in civil law jurisdictions where there is no concept of “privilege”, rather the lawyer is bound by rules of “professional secrecy” which will dictate the manner in which he or she must treat information given to him by the client.

5. National Privileges applicable to Funded Parties

The protections afforded to information (confidential or otherwise) passing between a lawyer and his/her client vary substantially across jurisdictions. The clearest distinction to be made is whether or not the jurisdiction concerned applies or requires a process of documentary “discovery” or “disclosure” (the sharing between opposing parties of documentary evidence) as a stage in the conduct of a dispute.

Discovery or disclosure processes most usually occur in the progress of a dispute within common law jurisdictions - England & Wales, Hong Kong, Australia and the US for example. The inevitable result of the requirement that parties share information and documentation is that the rules or laws around legal privilege – in respect of information and documents which can legitimately be withheld from that sharing process - have developed extensively. Broadly the starting point is that all relevant information and communications must be shared with opponents save for any information which is legitimately protected because it is privileged.

Many civil law jurisdictions have very limited or no process of discovery/disclosure in the course of a dispute. Nevertheless, the concept of “professional secrecy” has developed in order to protect from subsequent use or exposure confidential information which passes to a lawyer when a client seeks advice or instructs a lawyer on a dispute. The starting point is the opposite from that in common law jurisdictions: no information and communications need be or can be shared with opponents or other parties unless the prohibition is lifted (by client, lawyer, or authority, depending on the circumstances and the rules of the jurisdiction concerned).233

Despite this fundamental difference in approach, the broad policy behind protecting lawyer and client information and communications is the same across jurisdictions. A client must be able

233 The annexed reports reveal that the nature of professional secrecy, and the manner in which secrecy might be waived or lifted, varies widely. For example, it may be that the client has the right to lift the veil on secrecy and ask his lawyer to communicate secret information (Japan, Ukraine); the lawyer may have rights to lift of his own volition, for example where his/her life or honour is at threat or where imminent commission of a crime is suspected
to take advice and do business, having been candid about all of the applicable facts. Without the protection of law or legal doctrines like privilege and professional secrecy preventing the information from being released to the wider world, that process would not occur freely and openly.

A. Common law heads of privilege

Across the common law jurisdictions, litigation privilege and common interest are the “heads” which are most applicable to considerations of supplying information to funders, both during a funder’s due diligence to decide whether or not to invest, as well as in ongoing communications following an investment. Of course the precise treatment and categorisation of privilege across common law jurisdictions does vary.

Many common law jurisdictions divide the concept of legal privilege into legal advice privilege and litigation privilege. The US is an exception, with no concept of litigation privilege but instead a “work product doctrine” which covers lawyers’ work done in anticipation of litigation, or may be extended still further in some US states, such as California. Broadly, documents passing between a client and his lawyer forming part of the chain of information in order to seek and receive advice are protected by advice privilege; documents passing between client and lawyer or involving a third party, for the dominant purpose of proceedings (which may be litigation or arbitration) are covered by litigation privilege (and may, in the US context, count as “work product”).

1. Litigation or work product privilege

Litigation privilege protects communications with third parties, broadly where the dominant purpose of the communication is to further a litigation which is pending, reasonably

(Brazil, Portugal, Spain, Sweden) and this may be an automatic right, or one where permission of the local bar council, the court or other authority is required (Spain, Portugal). In many jurisdictions, disclosure of otherwise secret information to a third party will result in a loss of confidentiality and waiver of the right to secrecy unless attempts have been made through a confidentiality agreement to preserve secrecy.

234 In California, work product doctrine applies to any document prepared by an attorney in connection with his or her work as an attorney- there is no requirement that litigation be in contemplation. Conversely, the concept of attorney-client privilege in California is derived from statute and thus the Californian courts cannot expand upon the protection provided.

235 Legal advice/attorney-client privilege is not analysed in any more detail here as litigation privilege (or work-product privilege) is the more relevant head for communications with a funder. Indeed, whilst we understand that some US cases have held that there is no waiver of privilege when documents subject to advice privilege or attorney-client privilege are provided to a funder, this is still an area where funders themselves may exercise caution. See for example Burford Capital’s blog, Litigation Finance and attorney work product, of 18 September 2013 which states “we do not yet encourage disclosure to us of material that is not work product but is privileged; we’d rather be conservative in this area.” Clearly it is neither in the interest of the party, nor the proposed/invested funder to risk loss of privilege and potential exposure of information to the party’s opponent.

236 A funder currently engaged in funding a case would fall within the US version of the work product doctrine under federal Rule of Civil Procedure 26(b)(3)(A) for documents or tangible things created by the funder in anticipation of litigation or for litigation purposes. Federal Rule of Civil Procedure 26(b)(3)(A) states that "Ordinarily, a party may not discover documents and tangible things that are prepared in anticipation of litigation or for trial by or for another party or its representative (including the other party's attorney, consultant, surety, indemnitior, insurer, or agent)" unless there is a substantial need or undue hardship in obtaining information within the scope of discovery. A funder most likely falls within one of the categories "consultant, surety, indemnitior, insurer, or agent." Thus, the documents would be protected. If a funder declines to fund a case, however, then Rule 26 does not apply to the information that the funder had already obtained about the case, which means that this information remains
contemplated or existing. Whilst largely untested in common law courts, it should be possible to argue that sharing privileged information with a potential funder in order for it to decide whether to invest in the dispute meets that dominant purpose test, if it is the case that without funding the matter may not be pursued, or would be approached differently.

In the United States, there is a growing body of federal and state case law which suggests that the court will uphold the confidentiality (and thus privilege) of information passed to a funder. Documents prepared “because of” the litigation should be protected by work product privilege, thus documents prepared for funders, may still be privileged – even though a “dominant purpose” test might not be met. This is particularly where there is a confidentiality agreement in place.237

In the United States, there have also been cases in which work product privilege was found to apply to documents created “with the intention of coordinating potential investors to aid in future possible litigation.”238 That would suggest that documents created for approaches to multiple funders, most of whom will not, as a matter of logic, ultimately invest in a case, could meet the appropriate test for work-product privilege/ litigation privilege. However, one might argue that the privilege status of documents created solely for and provided to a funder who does not subsequently invest is more vulnerable to challenge;239 whereas once a funder is on board and a claimant could not pursue a matter without the continued investment by that funder, arguments as to the dominant purpose or reason for creating further communications are bolstered.240

That is on the basis that a funder is unlikely to agree to continue funding proceedings without progress updates; indeed funding agreements may well include a right of termination if the funder is not kept updated in the manner and frequency agreed. Thus the continued provision of information to the funder is crucial – and thus the sole or dominant purpose – as it allows the proceedings to continue. Nevertheless, the contrary is plainly arguable,241 so there must still remain a risk, particularly in jurisdictions deploying the dominant purpose test, that no privilege will apply.242

unprotected in the US. All jurisdictions should adopt a rule protecting the information of a party seeking funding even if the funder declines to fund a case.

237 Miller v Caterpillar, 10 C 3770, 6 January 2014, United States District Court, N.D. Ill.
238 Mondis Technology Ltd v LG Electronics Inc No2: 07-CV-565-TJW-CE 2011 WL1714304
239 We are unaware of common law decisions which make a clear distinction between the privilege status of communications with a funder who does invest, and one who does not. In Bray & Gillespie Mgmt LLC v Lexington Ins. Co. 2008 2008 WL 5054695 M.D. Nov 17, 2008, arguments that a deponent could withhold answers to questions about discussions held with a funder (which did not subsequently invest) by arguing both attorney-client and work product privilege, failed. However, those claims failed because of procedural mistakes during the deposition so this would appear to be an area of risk where there is no clear position. 240 Federal Rule of Civil Procedure 26(b)(3)(A) explicitly protects work product once a funder is on board with funding the case.
241 For the position in England & Wales, see Winterthur Swiss Insurance Company and other v AG (Manchester) Limited and others [2006] EWHC 839, in particular paragraphs 85 and 86 of the judgment. Counsel for the claimants argued that litigation privilege could not apply during the insurer’s due diligence period when deciding to cover or not, as obtaining insurance was a condition precedent to litigating. Thus no litigation could be contemplated until insurance was effected. On the other hand, counsel for the defendants saw the due diligence process to obtain insurance as an “intrinsic” part of the unified purpose of working towards litigation, such that litigation privilege should apply.
242 The Task Force did not locate any case law in England & Wales that deals with the funder position, so again assumptions may only be drawn by examining analogous situations. In Winterthur Swiss Insurance Company and other v AG (Manchester) Limited and others [2006] EWHC 839 the court considered whether litigation privilege applied to preliminary claim information prepared in order to decide whether or not an ATE insurer would cover a
To our knowledge, the scope of litigation privilege has been tested in the English Courts once by virtue of an application by the defendants for funding-related documents (including those evidencing the funding terms), in the matter of Excalibur Ventures LLC v Texas Keystone & Ors. [A full analysis of this case is available in the England & Wales report.] In an unreported judgment, Mr Justice Popplewell held that not all documents brought into existence for the purposes of actual or contemplated litigation will be protected by litigation privilege. The Judge refuted the wider formulation of litigation privilege advanced by Excalibur - that the funding documents were covered by litigation privilege because they were made for the dominant purpose of litigation - and said that if that were the case, “where a litigant buys a new suit in order to appear as a witness...all documents and information in relation to that purchase [would be] privileged because its dominant purpose was the conduct of the litigation.”

The judge agreed with previous authorities that it is the “use of the document or its contents in the conduct of the litigation which is what attracts the privilege” and endorsed the principle stated in Dadourian Group that “Litigation privilege...can include a communication between a client and his lawyer or between one of them and a third party which comes into existence after litigation is commenced or contemplated for the dominant purpose of obtaining information or advice in connection with such litigation or of obtaining evidence (or information which might lead to evidence) for use in the conduct of such litigation.”

The defendants were granted copies of Excalibur’s funding agreements that were found not to be privileged, and also to be directly relevant to the claims and defences pleaded in that case. It may be that the reasoning was based on the specific facts that meant the funding arrangement was found to be directly relevant to the merits of the dispute. The Court was content, however, for certain terms (including the success fee, settlement and termination provisions) to be redacted in response to the Excalibur’s contention that knowledge of a party’s funding arrangements might provide a “tactical advantage in relation to various aspects of the conduct of the litigation.”

claim: “If the policy was not issued there would be no litigation.” There was no conclusive result: it was found either that litigation privilege did not apply, or that if it did it was in the hands of the insurer. However, it was clear that documents prepared after the inception of the policy did have litigation privilege.

243 [2013] EWHC 2767 (Comm) (the application was heard in 2012).

244 International Inc. & Ors v Paul Simms & Ors [2008] EWHC 1784 (Ch) (which cross referred to the House of Lords decision in Waugh v British Railways Board [1980] AC 521) at para 86.
Two further English high court cases (Arroyo and RBS) examine whether communications with ATE insurers, and the resultant policies, could be subject to legal advice or litigation privilege, and an analogy can be drawn between the position for ATE and for professional funding.\(^{245}\) However, as discussed in the jurisdictional report for England & Wales, those judgments are conflicting, leaving the position under English law unclear (Arroyo finding that an ATE policy is likely to be covered by litigation and legal advice privilege, RBS finding that only those parts of an ATE policy may be privileged that would allow one to work out what legal advice had been given. In the RBS case the court stated clearly that “it is unlikely that privilege attaches to an ATE policy as such on either ground (litigation or advice), except to the extent... that parts of a policy (such as, possibly, the amount of premium...) may attract legal advice privilege, and require redaction on the basis that the relevant part might allow the reader to work out what legal advice has been given...”). Thus, there are however convincing arguments to be made by parties seeking to resist disclosure of such documents both on the grounds that they are not relevant to the substantive case in issue, but also that any contents of the documents which betray legal advice (for example, premium, termination provisions and procedure over settlement offers) should be redacted prior to disclosure as those discrete aspects are likely to attract legal advice privilege.

The Arroyo and RBS judgments show an acknowledgment by the English court of the potential tactical advantage to a party who successfully obtains disclosure of an ATE policy (or by analogy, funder) documents, and thus careful consideration will be given before making any such order. It is suggested that arbitral tribunals should be mindful of the same tactical advantages, and be cautious in ordering disclosure of such documents unless there are exceptional circumstances.

2. Common interest

Each of England & Wales, Australia, Hong Kong, Singapore and some – but not all – US states\(^ {246}\) also recognise the concept of “common interest” as a species of privilege (or more specifically as an exception to the rule that to pass privileged material to a third-party constitutes a waiver of privilege).

Under this view, passing privileged documents to a third-party ordinarily results in a loss of privilege, but privilege is retained where it can be shown that there is a “common interest” in the subject matter of the relevant communication or the proceedings to which the document relates. As noted above, in international arbitration practice under the IBA Rules of Evidence, the existence of waiver is generally not expected to be determined by reference to national rules and law. Nevertheless, where applicable, the common interest doctrine provides additional support for Principle 3 of this Chapter.

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\(^{245}\) See Arroyo v BP Exploration Co (Columbia) Ltd (unreported) approved judgment of 6 May 2010, and RBS Rights Issue Litigation [2017] EWHC 463 (Ch). There is an examination of both judgments in the national report for England & Wales.

\(^{246}\) See also the decision of Miller v Caterpillar (ibid) which, in the context of sharing documents with a third party funder, decided that common interest did not apply, as the interest shared between the parties must be a legal interest rather than a commercial one. Funders may wish to ensure the manner in which a common interest is drafted is not solely a commercial one, but funders should be careful not to manufacture a substantive interest in the underlying subject matter of the dispute merely to obtain shelter under the common interest privilege. A court would likely see straight through such an attempt.
Where privileged documents are disclosed to a third-party who has a common interest with the party entitled to the privilege, the document remains privileged. In England & Wales common interest privilege is not a freestanding form of privilege. It allows a party to share material that already has the protection of legal advice or litigation privilege with a third party who has a “common interest without waiving or losing that privilege.”

The common interest privilege derives from and is well established as between insureds and insurers.\(^{247}\) For example, in the English Winterthur case it was found that an insurer held a common interest in the policy holder’s litigation. Mr Justice Aikens explained that:

“where a communication is produced by or at the instance of one party for the purpose of obtaining legal advice or to assist in the conduct of litigation, then a second party that has a common interest in the subject matter of the communication or the litigation can assert a right of privilege over that communication as against a third party. The basis for the right to assert this “common interest privilege” must be the common interest in the confidentiality of the communication.”\(^{248}\)

Importantly, in the English Winterthur case, a distinction was made between documents created during the insurer’s due diligence (the “pre-ATE documents”) and those created after the inception of the policy (the “post-ATE documents”). The applicability of litigation privilege was unclear in respect of the pre-ATE documents but accepted for the post-ATE documents. Consequently the finding of common interest between insured and insurer was confined to the post-ATE period.

If seeking to assert that the claimant-funder relationship is analogous, then the periods of time – pre- and post- investment - may be similarly categorised. A similar analysis appears to have applied in the Australian Asahi case in which common interest was found not to apply, as at the time a confidential report was provided to the insurer there was no basis to say the insurer would cover the claim.\(^{249}\)

By analogy, where a funder has invested in a case and is provided with privileged information in order to monitor that investment, it may well follow that a common interest with the party can be asserted. Commentators have opined that the third-party funder would share a common interest in the confidentiality of a communication provided to it by a party to a litigation “as it has the common interest of pursuing litigation or arbitration in much the same way an insurer does”.\(^{250}\) However, there is more doubt over whether a common interest can be applied during a pre-investment due diligence phase.

There is also some argument to say that a funder-counsel relationship may not have the same attributes as the relationship with an insurer. The insurer’s rights of subrogation (and indeed express contractual rights) may contribute both to securing the insurer’s rights to otherwise

\(^{247}\) See Winterthur (ibid) in which an insurer was able to assert a common interest with an insured claimant at least for the post-ATE period. The Australian courts have treated the insurer-insured relationship similarly. See section 3 of the Australian jurisdictional report which refers to Spotless Group Ltd v Premier Building and Consulting Group Pty Ltd [2006] VSCA 201 and Asahi Holdings (Australia) Pty Ltd v Pacific Equity Partners Pty Limited (No. 2) [2014]FCA 481.

\(^{248}\) Winterthur Swiss Insurance Company & Anor v AG (Manchester) Ltd & Ors [2006] EWHC 839 at 78.

\(^{249}\) See the jurisdictional report for Australia, and reference therein to Asahi Holdings (Australia) Pty Ltd v Pacific Equity Partners Pty Limited (No2) [2014] FCA 481.

privileged documents and to emphasising a community of interest. Thus, care should be taken when drawing an analogy. Moreover, this appears to be largely untested in the courts of common law jurisdictions as we are not aware of decisions which examine the common interest doctrine specifically in respect of the funder-counsel relationship. Nevertheless, an assertion of common interest is a standard term within confidentiality agreements made between funders and parties before information is shared.

The U.S. national court case *Miller v Caterpillar* suggests that, at least in Illinois, \(^{251}\) the nature of the “common interest” will be relevant. Where the common interest between party and funder is commercial only, a communication will not be protected. The parties must be able to demonstrate a common interest in the legal aspects of the matter. Similarly, in *Leader Technologies v Facebook* Delaware took the same view that a funder does not fall within the common interest exception. \(^{252}\)

### 3. Confidentiality agreements/Limited waiver

Under English law, a party is able to share privileged material with a limited number of third parties pursuant to an express agreement to keep that material confidential, thus attempting to preserve its privileged status. There is not generally an intention to waive privilege as against the world at large, but to a limited, identified third party, such that this practice is known as “limited waiver”. Whether a waiver is limited is a matter of fact and degree, so caution must be taken in terms of parties (and their number) to whom a waiver is intended. \(^{253}\)

Parties intending to make a limited waiver should expressly state the basis on which a disclosure is being made in order to minimise the risk of a wider (unintended) loss of privilege. Nevertheless, even without clear wording, the courts of England & Wales have been prepared to impose limits and rescue a waiver after the event. \(^{254}\)

Where a common interest is in doubt, or does not apply, a limited waiver may be another method by which privileged information may be shared with a funder. Thus confidentiality agreements typically include wording as to intended limited waiver as an alternative, or in addition to, an assertion of common interest. Where there is no common interest, the party to whom a limited waiver of privilege is made cannot for himself assert privilege. Contrast this with common interest where the privilege is one which both common parties are entitled to assert. \(^{255}\) Similarly the US courts in the last few years appear broadly to have been accepting of the role of the third-party funder and have found that where: (i) appropriate confidentiality agreements are in place; (ii) there is an underlying privilege in the documents; and (iii) the sharing is “reasonably necessary” to advance the purpose for which the lawyer was consulted, the attorney-client

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\(^{251}\) In *Miller v Caterpillar* (17F. Supp. 3d 711 (N.D. Ill. 2014)) the United States District Court held that common interest does not apply and thus any attorney-client privilege protection which applied to documents was lost when those documents were passed to a third party funder. This was on the basis that the interest between sender and recipient must be a legal as opposed to a purely commercial one. As treatment of privilege and indeed the doctrine of common interest varies by US state, specific local advice must be taken.

\(^{252}\) 719 F. Supp. 2d 373 (D. Del. 2010).

\(^{253}\) See *Privilege*, PASSMORE, 3rd edition 2013, Sweet & Maxwell at 7-043 which discussed the issue of the point at which an intended limited waiver becomes too wide to preserve confidentiality and thus privilege as against the rest of the world.

\(^{254}\) See PASSMORE, ibid, at 7-038.

\(^{255}\) See Passmore on Privilege, ibid at 7-038 and its footnote 76.
privilege and work product privilege will be protected. This should be the case even where a common interest cannot be found to apply. Clients must provide privileged information under a limited waiver which is clearly worded, and in circumstances which protect the confidentiality of the information. In that way whilst privilege is waived as against the funder, it remains enforceable against the rest of the world. Nevertheless, clients and funders should be forewarned that the law in this respect varies from state to state, and most states do not explicitly protect information shared with funders. There are a three states, however, that explicitly protect information shared with funders via statute - Indiana, Nebraska, and Vermont - although those statutes were enacted in the context of consumer litigation funding rather than commercial funding or international arbitration.256

B. Civil jurisdictions – heads of “privilege”

“Privilege” is not a concept commonly adopted in civil jurisdictions. Instead the relationship between lawyer and client is seen as one of confidence and information passing between them is protected by a “professional secrecy” doctrine that applies with respect to both contentious and non-contentious work (and in some jurisdictions even includes pre-existing information or documents given to a lawyer in order for him to advise).

The secrecy concept, set out in professional rules, statutes, and civil procedure rules or otherwise, means that information relayed between lawyer and client cannot be revealed to the court, authorities or the wider world. In some civil law jurisdictions, such as South Korea, Turkey and the Netherlands, this doctrine forms part of counsel’s ethical obligations and in general cannot be waived by the client. In other jurisdictions, client consent or permission from a regulator/bar association may allow the lawyer to reveal information, for example in order to defend himself, or to make disclosures to a regulator or authority. In other jurisdictions (such as Russia, Ukraine and Brazil), a client may expressly or impliedly consent to his lawyer passing information on to a third-party (an insurer or funder for example) but otherwise the information retains its “secret” status.257

The release, with or without client consent, of information to funders may pose a risk to the inherent secrecy of the information, however. In some jurisdictions (such as Turkey, Portugal and Sweden) the information in the hands of a funder (as opposed to a lawyer) will not be subject to professional secrecy, so a funder may be obliged, for example by court order, to reveal that information. Alternatively, passing information to a funder will be seen as a waiver of the secrecy

256 See 2016 Ind. Acts 1557 (providing an exception to waiver of the attorney-client privilege and work product doctrine for communications between parties and funders in Indiana); VT. STAT. ANN. tit. 8, § 2255 (2016) (providing that “communication between a consumer’s attorney and the [funding] company shall not be discoverable” and providing an exception to waiver of the attorney-client privilege and work product doctrine for communications with funders in Vermont); NEB. REV. STAT. § 25-3306 (2010) (providing an exception to waiver of the attorney-client privilege and work product doctrine for communications with funders in Nebraska).

257 As noted above, in many civil jurisdictions a lawyer’s right and obligation to keep secret matters communicated by his client is derived from procedural rules but also professional obligations or the constitution of his/her jurisdiction, and is thus inviolable, save for limited policy exceptions and in some instances the ability of a client to lift such a restriction. Tribunals may need to allow for the assertion by a civil lawyer of his professional obligations with regards to secrecy of information, and ensure that decisions on the parameters of discovery do not violate that assertion. Moreover, civil lawyers must be careful to consider the mechanics of releasing secret information to a funder to ensure that the lawyer is not inadvertently breaching his obligations to keep client matters secret. See for example the reports in relation to The Netherlands, Germany, Turkey, Ukraine, Russia.
otherwise afforded to the information, and it may therefore be admissible as evidence or susceptible to disclosure to authorities on request. That risk may be alleviated by use of an appropriately worded confidentiality agreement.258

In advance of sharing information, then, funders and potential funded parties should take considered advice on whether and how some level of protection over the information may be maintained. As in common law jurisdictions, the role of the funder and the protections that may be afforded information passing to them is largely untested.

Likewise, some civil law jurisdictions are developing methods for extending privilege protections to third-party funders. Principally this includes the use of confidentiality agreements when releasing information to third-party funders in order to retain maximum control over the use of the information259. Consideration may also be given to whether it is the lawyer or client who passes on the information and/or whether the funder is simply copied into communications between lawyer and client in order to preserve secrecy. In some jurisdictions whilst the lawyer’s duty and right to assert professional secrecy may protect the communication with a third-party, the same will not apply to the client.260

It should nevertheless be noted that in certain civil jurisdictions information transferred by the lawyer to a third party will lose its confidential status regardless of the existence of a confidentiality agreement: once in the funder’s hands, the secrecy in the information itself is considered waived.261 This may depend on whether or not the client has expressly waived the secrecy.

C. To whom does any privilege belong?

1. Common law jurisdictions

In common law jurisdictions any privilege belongs to the client and is for the client alone to waive. No adverse inference can be drawn (for example by a court) from a client’s refusal to waive his right to assert privilege. Even where it may be in professional interests of an adviser to be able to waive privilege, it is for the client alone to waive. For example if the adviser is facing criticism or legal action by a third-party and would wish to deploy the privileged information in order to defend himself/herself, without permission of the client (or former client, as the privilege is permanent even after a case or matter is closed) the lawyer may take no steps to deploy or disclose the privileged information. Where the client himself/herself brings a claim against his/her

258 The effectiveness of a confidentiality agreement may vary across jurisdictions, and between litigation and arbitration. In Russia, for example, whilst a confidentiality agreement may protect secrecy from third parties, this may be irrelevant if a court makes an order that documents should be disclosed and used in evidence in court proceedings. Within arbitration, the sensible approach in order to ensure that secrecy remains intact is that the advocate retains custody over relevant documents; alternatively that the funder instructs its own advocate who holds the documents.

259 The use of confidentiality agreements appears to offer effective protection for secret information in the hands of the funder in jurisdictions such as the Netherlands, Russia, Germany and Japan.

260 In Germany for example, whilst a communication (with a client’s permission) between a lawyer and a funder would be protected as long as an appropriate confidentiality agreement was made, a direct communication from the client to the funder could not be protected in any way. Contrast with Japan, Sweden and Spain where it would appear that either a lawyer or client could communicate with a funder without risk of waiver or loss of the confidential status of information. Interestingly, in the Ukraine, a communication by lawyer to funder without express permission from a client would be inadmissible evidence and thus it is preferable for communications to come at all times from lawyers.

261 See for example the jurisdictional reports for Turkey and Portugal.
lawyer, then he/she is regarded as having waived the privilege and confidence to the extent required for the lawyer to defend himself/herself.

Civil law jurisdictions

The balance between the rights and duties of lawyers and their clients is different in civil jurisdictions from that in common law jurisdictions where the client is in complete control; in addition there are differences of approach according to jurisdiction.

Where professional secrecy applies, it may be regarded both as a duty of the lawyer to keep matters secret, but also a right to be exerted, for example in order to resist giving testimony on the matters which are subject to the secrecy for example. Generally, unless the secrecy is waived by the client, or there is permission from the lawyer’s regulating body (such as a local bar council) the lawyer is able to resist all requests for disclosure.

2. Documents held by the funder

There is a further concern that documents created and/or held by the funder are protected. Again, the problem must be analysed both in the context of common law jurisdictions and civil law jurisdictions.

Common law: Where a funder, in order to decide to invest or not, consults its own external lawyers, then it should naturally follow that the flow of information seeking and obtaining that advice is covered by advice privilege or its equivalent across common law jurisdictions such as attorney-client privilege in the US. The situation where a funder consults its own employees who are lawyers for that same advice requires additional consideration. If properly consulted in his or her capacity qua lawyer (rather than as a commercial adviser) then most common law jurisdictions would recognise that the resultant documentation was equally covered by advice privilege or its equivalent. This does highlight, however, the need for funders themselves to consider privilege issues carefully in the structure of their business and the way they deploy employees with a legal qualification.

Any other documents generated by a funder – but not by lawyers – would be unlikely to attract the protection of advice privilege, but would likely be covered by litigation privilege/work-product privilege, if its production can be argued to meet the dominant purpose test (or the less onerous “because of” test for the US) discussed above. However, this may be susceptible to challenge, for example in situations where a funder does not ultimately make an investment in the proposed litigation or where it is asserted that the information was passing for a commercial rather than a legal purpose, as may well be the case with a funder.

Civil law: the position is much less

262 For example, in the US under Federal Rule of Civil Procedure 26(b)(3)(A).

263 See the analysis by Grace M. Giesel in Alternative Litigation Finance and the Work-Product Doctrine, Wake Forest Law Review, Vol 47, 2012, 1083-1140, in particular at 1124-1125 in which there is an examination of analogous cases of evaluation of ongoing litigation by an independent company auditor. Where those evaluations included and recorded the thoughts and impressions of lawyers advising the company, the court was prepared to find that work-product privilege applied. (United States v Deloitte LLP, 610 F 3d 129 (D.C. Cir 2010). The court in that case was able to apply the less stringent “because of” test and found that the documents recorded information “...prepared by the company and its lawyers because of the prospect of the litigation.” This may be seen as a judgment at the limits of the because of test, and such protection may not be forthcoming in other courts of common law jurisdictions, but nevertheless the case highlights the policy motivations of courts to protect the confidentiality of the adversarial litigation or arbitration process, even if that is to go as far as to protect documents created by a funder.

264 Professional ethics rules would usually currently prohibit a lawyer from using or revealing any information gleaned from a prospective client even if that lawyer does not take the client’s case. See e.g. the American Bar
clear in civil jurisdictions as the precise structure of the professional secrecy rules vary across jurisdictions and depends on: the professional status of the person to whom information is given; the rights of the client to circulate information; and the ability of either professional or client to lift the secrecy obligation/ right in certain circumstances. Many civil jurisdictions will not view a funder as belonging to a profession which of itself attracts the status which confers professional secrecy rights and obligations, so this may mean that the only chance of asserting secrecy is for the funder to appoint its own lawyers to consider the case and proposed investment and thus take advantage of the secrecy status of those lawyers. Other jurisdictions, for example Brazil, recognise certain financial institutions as structures which may attract professional secrecy, so it may be that a funder could incorporate itself as a particular type of financial entity in order to take advantage of the additional status this would confer on communications.

There is a further concern that the funder itself keep the information confidential and does not share information it has from one party/client with another party/client without consent. In England & Wales, where many of the major funders are self-regulated under the Association of Litigation Funders, comfort can be taken from Article 7 of the ALF Code of Conduct which provides that “A funder will observe the confidentiality of all information and documentation relating to the dispute to the extent the law permits, and subject to the terms of any confidentiality or non-disclosure agreement agreed between the funder and the funded party. For the avoidance of doubt, the funder is responsible for the purposes of this code for preserving confidentiality on behalf of any Funder’s Subsidiary or Associated Entity.” Equivalent provisions can be added to the confidentiality agreement entered into with the funder.

A related question is whether a funder can refer to otherwise confidential information in its possession to defend itself in a suit by the funded party. The answer is presumably yes in most circumstances.\(^{265}\)

Again, English insurance cases can provide a helpful analogy. In *Formica*\(^{266}\) ECGD had guaranteed 90% of the loss arising out of a contract between Formica and a Swedish company. The latter went into liquidation and Formica called on the guarantee. ECGD resisted on the basis that it was not kept apprised of the litigation developments which they had initiated overseas to try and recover some of the debt in breach of a condition of the guarantee. The court held that Formica could not claim legal professional privilege in relation to those documents in the litigation since ECGD was contractually entitled to see them at the time the guarantee was active.\(^{267}\) Their

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\(^{265}\) But see, for example, the most recent Court of Appeal authority, *Berezovsky v Hine & Ors* [2011] EWCA Civ 1089, the Court held that Mr Berezovsky could assert privilege in his draft witness statement in the context of later, separate proceedings despite having given it to the Defendant in earlier unrelated proceedings. Importantly, when the document was initially disclosed, there was no express restriction as to the purpose for which the privileged document could be used and the court inferred this restriction from the “obvious intentions of the parties.” The Court held that privilege could be retained by the claimant in relation to documents in the litigation since ECGD was contractually entitled to see them at the time the guarantee was active.\(^{267}\)

\(^{266}\) *Formica Ltd v Secretary of State* (acting by the Export Credits Guarantee Department) [1995] 1 Lloyd’s Rep. 692

\(^{267}\) The court held that “where such documents never were transferred, but, if they had been, would have been transferred for such a joint interest purpose, the applicant for discovery can show that had he been supplied with the documents at the time, he would have held them subject to the mutual obligations of confidence attributable to legal
contractual relationship meant that both parties had a common interest in recovering the outstanding debt from the Swedish company.  

3. Risk that privileged documents are sought in litigation proceedings

There is a risk that a party to an arbitration may turn to the courts to try to seek disclosure of confidential information in the hands of a funder. For example, Article 17J of the UNCITRAL Model Law provides that a court “shall have the same power of issuing an interim measure in relation to arbitration proceedings, irrespective of whether their place is in the territory of this State, as it has in relation to proceedings in Court.”

The Model Law provision clearly envisages that a court in the relevant jurisdiction has the power to order discovery as an interim measure. There has, for example, in recent years been a proliferation of attempts to use the 1782 procedure in the US court to seek US-style disclosure of documents held by a third party in aid of arbitration. Section 1782(a) provides in relevant part:

“The district court of the district in which a person resides or is found may order him to give his testimony or statement or to produce a document or other thing for use in a proceeding or a foreign or international tribunal, including criminal investigations conducted before formal accusation. The order may be made pursuant to a letter rogatory issued, or request made, by a foreign or international tribunal or upon the application of any interested person and may direct that the testimony or statement be given, or the document or other thing be produced, before a person appointed by the court…. The order may prescribe the practice and procedure, which may be in whole or part the practice and procedure of the foreign country or the international tribunal, for taking testimony or statement or producing the document or other thing. To the extent that the order does not prescribe otherwise, the testimony or statement shall be taken, and the document or other thing produced, in accordance with the Federal Rules of Civil Procedure.”

There is a divergence of authority as to whether this section can be used in support of arbitration proceedings. Nevertheless, there is a risk that an opponent in a dispute could attempt to use such mechanisms to obtain documents by seeking them directly from a funder. For these reasons, extra caution should be exercised to minimise the risk that such applications could be successful. It is professional advice. He is thus entitled to say that he would then have been within the ambit of confidentiality protected by the law and that therefore privilege does not attach to the documents which he now seeks on discovery.”

268 Similarly, in other insurance cases like Commercial Union Assurance Co v Mander and Winterthur, [1996] 2 Lloyds Rep 640, the Courts have shown that the insured cannot use privilege to prevent his insurer from accessing privileged documents (given its contractual entitlement to them) and neither can an insurer withhold such documents from a reinsurer on the grounds of privilege. Cia Barca de Panama SA v George Wimpey & Co Ltd [1980] 1 Lloyd’s Rep 598, 615, involved the scenario where privileged material existed in connection with a case in which A and B were both involved in at the same time. Lord Bridge said that if “A and B have a common interest in litigation against C and if at that point there is no dispute between A and B then if subsequently A and B fall out and litigate between themselves and the litigation against C is relevant to the disputes between A and B then in litigation between A and B neither A nor B can claim legal professional privilege for documents which came into existence in relation to the earlier litigation against C.”

269 See the discussion by Jonathan Blackman and Peter Fox in Global Arbitration Review, 16 August 2016, “Discovery in Aid of Arbitration under 28 USC 1782, in particular the discussion on the cases of NBC v Bear Stearns & Co 165 F.3d 184, 191 (2nd Cir. 1999); Republic of Kazakhstan v Biedermann International 168F 3d 880 (5th Cir 1999)against such use, and Intel 542 U.S. 198 (2004) in support. In the First, Third, Eighth and DC Circuits, district courts have held that at least some types of private arbitral tribunal are within the ambit of the statute, while their counterparts in the Fifth, Seventh, Ninth and Tenth Circuits have held that at least some types of private arbitral tribunal are not covered. In one instance, the same arbitration proceeding has produced conflicting decisions in different district courts.
imperative to take steps to consider possible avenues of privilege protection, make clear assertions of such protection, and put in place clear contractual provisions to keep information confidential.
Chapter 6†

COSTS AND SECURITY FOR COSTS

PRINCIPLES

Final award (allocation) of costs:

1. Generally, at the end of an arbitration recovery for costs should not be denied on the basis that a party seeking costs is funded by a third-party funder.

2. When recovery for costs is limited to costs have been “incurred” or “directly incurred,” the obligation of a party to reimburse the funder in the event of successful recovery is generally sufficient for a tribunal to find that a funded party comes within that limitation.

3. In the absence of exceptional circumstances, the cost of funding, including a third-party funder’s return, is ordinarily not recoverable as costs.

4. Generally, a tribunal lacks jurisdiction to issue a costs order against a third-party funder.

Security for costs:

1. Applications for security for costs should be determined irrespective of any funding arrangement and on the basis of impecuniousness.

2. In the first instance, the burden is on the moving party; no party should have to defend a motion for security unless and until the moving party makes a prima facie showing of impecuniousness.

3. If a party is found to be impecunious, that party should be given the opportunity to present additional evidence of funding or have a security for costs award imposed.

4. At that stage, a request for disclosure of third-party funding agreements should normally be accepted as the moving party and the tribunal should be able to examine the relevant parts of the third-party funding agreement (in particular provisions on the funder’s termination of funding rights and funder’s obligation to cover adverse costs) in the context of the security for costs application against an impecunious party. However, tribunals should limit disclosure orders to the provisions that are strictly

† Primary contributors to this Chapter included: Stavros Brekoulakis, Audley Sheppard, Susan Dunn, Mick Smith and Jonas von Göler.
necessary to assess the extent to which the funder may cover (or not) an adverse costs order.

5. If a tribunal decides that a security for costs order is warranted, it can order security for costs by way of a bank guarantee. Payment into a bank account may be ordered for security for costs in exceptional circumstances, and where there is no ATE or any other form of evidence of indemnification arrangements already in place.

6. In addition, an arbitral tribunal should consider indicating to the requesting party that, should the defence fail, it will be held liable for the costs reasonably incurred by the funded party in posting security. It should be for the funded party to substantiate the amount of costs it reasonably incurred in posting security.
I. INTRODUCTION

The purpose of this Chapter is to provide guidelines in respect of the impact of TPF on allocation of costs and security for costs applications. The report focuses on non-recourse funding arrangements. When relevant, ATE, BTE and contingency fee arrangements are discussed for purposes of comparison. The Chapter first examines issues on awarding of costs, and then issues on security for costs applications. Unless a tribunal establishes the likelihood that costs could in principle be awarded against an unsuccessful claimant, it cannot make a decision on a security for costs application.

1. Awarding of Costs

When awarding costs at the end of the proceedings, an arbitral tribunal has to address a number of issues. First, it must decide whether to award costs... Second, if costs will be awarded, how they should be allocated. Third, where costs are allocated based on the outcome of the case, the tribunal must determine which of the prevailing party’s costs are recoverable (type and amount of recoverable costs). An arbitral tribunal’s decisions on these issues will be framed by the applicable arbitral laws and rules [A]. A number of arbitral tribunals (and state courts) have already dealt with the awarding of costs in the presence of a third-party funding agreement. These decisions shall be looked at [B] before presenting the recommendations of the sub-committee on how Tribunals should award costs in claims funded by third-party funders [C].

The Report addresses the following issues:

1. Should a funded party that has prevailed in the arbitration be able to recover party costs at all where these costs have been funded by a third party?
2. Where costs are allocated based on the outcome of the case and the funded party prevails, what type of costs can it recover from the opponent?
3. Where costs are allocated based on the outcome of the case and the non-funded party prevails, could an arbitral tribunal render a costs order directly against a third-party funder?

[A] Arbitral Laws and Rules

i. Arbitral Laws
English arbitration law contains comparatively detailed provisions on costs allocation. Section 61 of the English Arbitration Act 1996 provides that:

(1) The tribunal may make an award allocating the costs of the arbitration as between the parties, subject to any agreement of the parties.

(2) Unless the parties otherwise agree, the tribunal shall award costs on the general principle that costs should follow the event except where it appears to the tribunal that in the circumstances this is not appropriate in relation to the whole or part of the costs.

As regards the amount of recoverable costs, Section 63 of the English Arbitration Act 1996 states:

(3) The tribunal may determine by award the recoverable costs of the arbitration on such basis as it thinks fit.

If it does so, it shall specify—

(a) the basis on which it has acted, and
(b) the items of recoverable costs and the amount referable to each.

(4) If the tribunal does not determine the recoverable costs of the arbitration, any party to the arbitral proceedings may apply to the court (upon notice to the other parties) which may—

(a) determine the recoverable costs of the arbitration on such basis as it thinks fit, or
(b) order that they shall be determined by such means and upon such terms as it may specify.

(5) Unless the tribunal or the court determines otherwise—

(a) the recoverable costs of the arbitration shall be determined on the basis that there shall be allowed a reasonable amount in respect of all costs reasonably incurred, and

(b) any doubt as to whether costs were reasonably incurred or were reasonable in amount shall be resolved in favour of the paying party.

Default rules on costs shifting can also be found in the arbitration laws of Hong Kong, Germany, Spain, Brazil and Portugal. While the arbitration laws of the UNCITRAL Model Law, France, Switzerland, and the United States are silent on the issue of costs allocation, it is clear that tribunals sitting in these jurisdictions have the power to render awards on costs.

ii. Arbitral Rules

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270 Hong Kong Arbitration Ordinance (2011), s. 72(4) (written offer to settle as a particularly relevant factor); German Code of Civil Procedure (2013), s. 1057(1) (outcome of the case as a particularly relevant factor); Spain: Law 60/2003, Art. 37; Portugal: Law 63/2011, Art.42; Brazil: Law 13.129 (26 May 2015) Art.27.
Many widely used arbitral rules set a presumption that costs should follow the event, or should be allocated based on the degree of success, unless particular circumstances call for a different approach.271 Other rules simply provide for wide arbitrator discretion.272

As regards the type and amount of recoverable party costs, Article 40(2)(e) UNCITRAL Rules is representative, limiting recoverable costs to ‘[t]he legal and other costs incurred by the parties in relation to the arbitration to the extent that the arbitral tribunal determines that the amount of such costs is reasonable’. Similar formulations can be found, for instance, in the ICC Rules,273 the LCIA Rules,274 and the CIETAC Rules275

iii. Arbitral Practice

Since the procedural matrix established by the arbitration law and rules typically allow tribunals wide discretion as regards costs allocation, it is not always easy to predict how an arbitral tribunal will ultimately approach the issue in a given case. The award of substantial costs based on the case’s outcome – notably of legal costs based on counsel’s hourly fees – constitutes an approach that is especially prevalent in court litigation in the United Kingdom and other common law jurisdictions. Nevertheless, it is one that appears to be increasingly applied in international arbitration as well, not least since, as discussed above, many widely used arbitral rules provide that the prevailing party is presumptively entitled to its costs, while authorizing the tribunal to adopt a different standard if appropriate in the particular case.276

271 UNCITRAL Rules (2010), Art. 42 (‘costs of the arbitration shall in principle be borne by the unsuccessful party’); LCIA Rules (2014), Art. 28(4) (‘costs should reflect the parties’ relative success and failure in the award or arbitration or under different issues, except where it appears to the Arbitral Tribunal that in the circumstances the application of such a general principle would be inappropriate under the Arbitration Agreement or otherwise’); DIS Rules (1998), s. 35(2) (‘[i]n principle, the unsuccessful party shall bear the costs of the arbitral proceedings’, but the tribunal may order each party to bear its own costs or apportion the costs between the parties, in particular, where each party is partly successful and partly unsuccessful); WIPO Rules (2014) Art. 74.

272 ICSID Convention, Art. 61(2) (‘the Tribunal shall, except as the parties otherwise agree, assess the expenses incurred by the parties in connection with the proceedings, and shall decide how and by whom those expenses, the fees and expenses of the members of the Tribunal and the charges for the use of the facilities of the Centre shall be paid’); SIAC Rules (2016), Art. 35(1) (‘[u]nless the parties have agreed otherwise, the Tribunal shall determine in the award the apportionment of the costs of the arbitration among the parties’); ICC Rules (2017), Art. 38(5) (‘[i]n making decisions as to costs, the arbitral tribunal may take into account such circumstances as it considers relevant, including the extent to which each party has conducted the arbitration in an expeditious and cost-effective manner’).

273 ICC Rules, Art. 38(1) (‘reasonable legal and other costs incurred by the parties for the arbitration’).

274 LCIA Rules (2014), s. 28(3) (‘legal or other expenses incurred by a party ... The Arbitral Tribunal shall decide the amount of such Legal Costs on such reasonable basis as it thinks appropriate’).

275 CIETAC Rules, Art. 52(2) (winner entitled to ‘the expenses reasonably incurred by it in pursuing the case’).

[B] Costs Decisions in Third-Party Funding Scenarios

This section looks at the body of arbitral case law dealing with the awarding of costs in the context of third-party funding.

i. Kardassopoulos v. Georgia

In Ioannis Kardassopoulos & Ron Fuchs v. Georgia\textsuperscript{277} the investors were successful in an arbitration funded by German company Allianz Litigation Funding for a claim against Georgia for compensation for the unlawful termination of a concession to build and maintain a pipeline. Claimants requested that they be awarded costs of proceedings including legal costs, arguing that there is a trend of outcome-based recovery in investment-treaty arbitration. Respondent argued, \textit{inter alia}, that claimants’ legal costs were excessive. Respondent also argued that it appears that the claimants’ legal costs might have been born (at least in part) by a third-party investor and therefore not properly recoverable. The Tribunal held that:

The Tribunal knows of no principle why any such third party financing arrangement should be taken into consideration in determining the amount of recovery by the Claimants of their costs.\textsuperscript{278}

This passage has been adopted by the ICSID annulment committees in \textit{RSM v. Grenada}\textsuperscript{279} and \textit{ATA v. Jordan}\textsuperscript{280}.

ii. Siag and Vecchi v. Egypt

In \textit{Siag and Vecchi v. Egypt}\textsuperscript{281} the claimants’ law firm (King & Spalding) had acted on a contingency fee basis. Despite this, the claimants requested recovery of a specified amount of normal (hourly) fees, without the corresponding invoices or other details. The tribunal accepted this. Orrego Vicuna dissented, albeit not on the issue of substantiation of costs, but more generally on the allocation of costs:

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\textsuperscript{277} \textit{Kardassopoulos and Fuchs v. The Republic of Georgia} (ICSID Case Nos. ARB/05/18 and ARB/07/15), Award (3 March 2010).
\textsuperscript{278} Ibid., para. 691.
\textsuperscript{279} \textit{RSM Production Corporation v. Grenada} (ICSID Case No. ARB/05/14), Annulment Proceeding, Order of the Committee Discontinuing the Proceeding and Decision on Costs (28 April 2011) para. 68.
\textsuperscript{280} \textit{ATA Construction, Industrial and Trading Company v. The Hashemite Kingdom of Jordan} (ICSID Case No. ARB/08/2), Annulment Proceeding, Order Taking Note of the Discontinuance of the Proceeding (11 July 2011) para. 34.
\textsuperscript{281} \textit{Siag and Vecchi v. The Arab Republic of Egypt} (ICSID Case No. ARB/05/15) Award (1 June 2009).
In respect of the costs of this arbitration I believe that a more adequate approach would be to require each party to pay one half of such costs, particularly taking into account the fact that the Claimant agreed to pay attorney’s fees only on a successful recovery. While there is nothing unusual in such arrangement, it entails the acceptance of the Claimant of a degree of risk that should not entirely be shifted to the Respondent, particularly in view of the amounts involved.282

iii. Quasar de Valores v. Russia

In Quasar de Valores v. Russia the tribunal denied the prevailing Spanish portfolio investors in Yukos recovery of their costs because the funder (Menatep, ex-majority shareholder in Yukos) had funded the entirely the costs of the proceedings and had no contractual right vis-à-vis the claimants for reimbursement of these costs. The tribunal explained that:

The usual arguments about the recoverability of costs where a party’s representation in a case has been financed by a third party are inapposite here, because such third-party financing is typically part of a legally enforceable bargain under which the prevailing party in the arbitration has given up something in return for that support. Here, it is conceded that there is no legal duty on the part of the Claimants to hand over any recovery on account of costs to Menatep.283

As flagged in the extract from the ruling of the tribunal, above, the factual circumstances in Quasar de Valores were highly unusual in that the funded party had no obligation whatsoever to reimburse the funder for the costs advanced, effectively giving the funded party a “total free ride”.284

iv. ICC Case No. 7006

By contrast to Quasar de Valores v. Russia, an ICC tribunal noted (obiter) that the legal costs of a respondent that had been paid by a third party (insurer) would have been recoverable had the respondent succeeded:

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I believe that they are [recoverable], at least from the point that Defendants rather than the
[indemnifier], mandated counsel to represent them in the arbitration. By so doing, they
incurred the primary obligation to pay such counsel’s fees and expenses—one not negated
by the fact that someone else, through prior arrangement, paid them on their behalf. The
counterpart to this determination is that Defendants would be obliged to reimburse their
indemnifier any costs they recovered from the arbitration.285

v. Overview of Recoverability of funding Costs in Litigation

For comparative purposes, this section provides a brief overview of the status of
recoverability of funding costs in litigation in some of the most popular jurisdictions for
international litigation.

As regards the question of whether a third-party funder may be ordered to pay adverse
costs should the funded claim fail, there is case law from the UK286 and the US287 to the effect that
costs can be awarded against third-party funders if they have obtained a sufficient degree of
economic interest and control in relation to the claim. It is doubtful whether the reasoning of these
litigation cases can readily apply to arbitration, which is consensual in nature; this is addressed
further below.

In England and Wales conditional fees and the premium for after-the-event insurance were
made recoverable under the English and Wales Courts and Legal Services Act as amended by the
made in any proceedings might include success fees. Section 58A(4) made it clear that the term
‘proceedings’ included arbitration proceedings. Section 29 Access to Justice Act 1999 provided
that ‘[w]here in any proceedings a costs order is made in favour of any party who has taken out an
insurance policy against the risk of incurring a liability in those proceedings, the costs payable to
him may, subject in the case of court proceedings to rules of court, include costs in respect of the
premium of the policy.’ This was subsequently changed with the Legal Aid, Sentencing and
Punishment of Offenders Act 2012, which abolished the recoverability of after-the-event insurance

285 Supplier v First distributor, Second distributor (ICC Case No. 7006), Final Award (1992) 4 ICC Bull.
(May 1993) 49.
286 Excalibur Ventures LLC v. Texas Keystone Inc. & Ors v. Psari Holdings Limited & Ors, English High
Court (Queen’s Bench, Commercial Court), (Case No. 2010 Folio 1517), Order of 23 October 2014, [2014] EWHC
3436, paras 4, 161 confirmed by the Court of Appeal in Excalibur Ventures LLC v Texas Keystone Inc & Ors [2016]
EWCA Civ 1144; Arkin v. Borchard Lines Ltd. & Ors, English Court of Appeal, Judgement of 16 May 2005, [2005]
EWCA Civ. 655 (‘[w]here … the non-party not merely funds the proceedings but substantially also controls or at any
rate is to benefit from them, justice will ordinarily require that, if the proceedings fail, he will pay the successful
party’s costs’). Further, the Arkin case is also considered authority to the effect that the funder’s maximum liability
for the respondent’s costs is capped at twice the amount loaned.
287 Abu-Ghazaleh v. Chaul, Florida Third District Court of Appeal, (Nos. 3D07–3128, 3D07–3130) Decision
of 2 December 2009, 36 So. 3d 691. Whereas parties litigating in front of US courts typically have to bear their own
costs, Abu-Ghazaleh v. Chaul presents special circumstances in that a fee shifting statute applied.
premiums and conditional fees for agreements entered into after 1 April 2013 on the ground that such premiums and fees were key drivers behind the escalating costs of civil litigation. In the United States – where parties typically bear their own costs – the Supreme Court has clarified that if a federal fee shifting statute applies and the prevailing party seeks to recover its contingency fees, only reasonable hourly fees (lodestar-method) are recoverable. In Germany, interest charged on a loan used to pay litigation expenses is not recoverable under section 91 German Code of Civil Procedure, since the interest cost is not directly related to the conduct of the proceedings. Accordingly, recovery of other funding costs (such as an after-the-event insurance premium) would likely be impossible from the perspective of German procedural law.

C. Key Observations and Suggestions of the Sub-Committee

For the purposes of this report it is assumed that, as is typically the case, a third-party funder assumes an obligation to reimburse the funder for the costs advanced, in case of successful recovery. It is also assumed that the tribunal is generally willing to allocate costs based on the outcome of the case.

[1] Should a funded party that has prevailed in the arbitration be able to recover party costs at all where these costs have been funded by a third party?

[a] Amount of costs: did a funded party ‘incur’ costs?

Although the answer to this question will depend on the billing structures adopted by third-party funders for each case, when a party is funded by a third-party funder it typically assumes an obligation to reimburse the funder for the costs advanced. The obligation to reimburse a funder should be sufficient for tribunals to accept that a funded party has incurred costs.

Specifically, the usual practice in funded arbitration claims is that the invoices by lawyers are issued in the funded party’s name and become payable by the funder as a result of the funding agreement. The funded party’s lawyers would usually send the invoice to the funder (along with a monthly report). If the funded party and funder are satisfied that the invoice is consistent with the pre-agreed budget, the funder will pay the invoice directly to the lawyer. Thus, the involvement of a funder does not change the funded party’s primary liability to discharge the bill. The funded party incurs the obligation to reimburse the funder for the costs so advanced in case of successful recovery (plus a return to the funder as per the funding agreement). For these reasons, the fact that the funder pays the bills is not practically speaking giving the opposing party a ‘free ride’ on not having to repay any costs if it ultimately fails to defend the claim against it.


289 Schulz, in MüKo ZPO, § 91 para. 205 (with further references); Herget, in Zöller, § 91 para. 13.
Equally important, if we accept, on a policy level, that third-party funding has an important role to play in supporting the system of international arbitration and providing access to justice for meritorious claims,\textsuperscript{290} it would be unwarranted to increase the costs of obtaining third-party funding. Claimants could potentially be discouraged from seeking funding if they know that they might not be able to recover potentially substantial legal costs, even in case of success.

It is therefore suggested that legal costs that the funded party is contractually obliged to repay to the funder should be considered as legal costs incurred by the funded party.\textsuperscript{291} Equally, and for illustrative purposes, other types of third-party funding, including traditional funding on a recourse basis, may not be considered a basis for denying an award on costs for the successful funded party.

For example, a P&I and FD&D Club will be responsible for paying the party’s legal expenses albeit they will not appear on the record. P&I and FD&D are a form of liability insurance.\textsuperscript{292} It operates on a “pay to be paid” principle, i.e. the member must incur a liability first and then the club will reimburse such expenses. In both cases the funded party pays the invoices to the legal representatives and then the club reimburses. Therefore, again the party on the record incurs the costs, and P&I and FD&D arrangements should not be considered a basis for refusing a costs award in favour of the successful party.

The same applies for conditional (or contingency) fee arrangements. CFAs\textsuperscript{293} typically provide that the successful party will have to pay the law firm the amount of time spent in the arbitration on the basis of its normal hourly rates and an uplift (i.e. a success fee). While recoverability of the uplift may be dependent on the circumstances of the case (see below under b), recoverability of the amount of the fees for the time spent in the arbitration by the legal firm should be possible as part of the legal costs incurred the successful funded party.

On the other hand, obtaining an ATE\textsuperscript{294} policy will not include any funding of the arbitration, and therefore the question of whether an ATE insurer pays the insured party its

\textsuperscript{290} As has been suggested, for example, the UK’s Civil Justice Council report endorsing the potential of litigation funding to increase access to justice, Civil Justice Council Report, “Improved Access to Justice—Funding Option & Proportionate Costs” (2007) <https://www.judiciary.gov.uk/wp-content/uploads/JCO/Reports/CJC/Papers/CJC-Improved-access-to-Justice—Funding-Options-and-Proportionate-Costs.pdf> (last accessed 18 August 2017); Cf also the UK Court of Appeal’s decision in the well-known \textit{Excalibur Ventures LLC v Texas Keystone Inc and others} \[2016\] EWCA Civ 1144, stating that litigation funding is “an accepted and judicially sanctioned activity perceived to be in the public interest” (per LJ Tomlinson). Cf also Lord’s Jackson’s Review of Civil Litigation Costs (in the UK) which allowed third party funding after it expressed concerns that “in some areas of civil litigation costs are disproportionate and impede access to justice”, Lord Rupert JACKSON, “Review of Civil Litigation Costs” (2009) Foreword, available at <https://www.judiciary.gov.uk/wp-content/uploads/JCO/Documents/Reports/jackson-final-report-140110.pdf> (last accessed 19 August 2016).


\textsuperscript{292} See Chapter 3 for definitions of P&I and FD&D.

\textsuperscript{293} See Chapter 3 for definition of CFAs.

\textsuperscript{294} See Chapter 3 for definition of ATE.
arbitration costs does not arise in the first place. ATE policies typically meet adverse costs awards only, and therefore the claimant will have to obtain funding from elsewhere or fund the arbitration itself. If it is successful, a party with ATE policy will have incurred legal costs, which should be recoverable.

[b] Allocation of costs: should a tribunal deviate from otherwise applicable outcome-based methods of costs allocation if the prevailing party’s costs have been funded?

The fact that a party’s costs have been paid by a third-party funder should not generally be regarded as a relevant factor in determining whether or not costs are to be allocated based on the outcome of the case. As explained in the previous section, these costs are incurred by the funded party who typically is obliged, under the funding agreement, to repay the funder if it is successful in the claim. Otherwise, the funded party would be left uncompensated for the costs it has incurred which it would have recovered had it not been funded.

[2] What amount and type of ‘costs’ can a prevailing funded party recover?

Funding arrangements will typically require the funded party not only to reimburse the funder for the actual arbitration costs covered, but also to pay for the cost of that capital, i.e. the funding costs (such as a conditional fee, or a litigation funder’s return) over and above normal legal costs.

Depending on the circumstances, the successful funded party might be able to claim funding costs as damages against the unsuccessful party in a separate claim. However, the requirements for causation and foreseeability would be difficult tests to meet under most national substantive laws.295

It would seem more reasonable for the successful funded party to attempt to recover funding costs from the unsuccessful party as part of the costs allocation exercise at the end of the arbitration, although the question whether an arbitrator can and should allocate funding costs is disputed.

In a survey of practice of arbitral tribunals under the ICC Rules, the ICC Report on Costs in International Arbitration states that funding costs, including the third-party funder’s success fee may be recoverable in certain circumstances.296

Further, there is recent authority for arbitration conducted in England under the English Arbitration Act suggesting that when funding costs are necessary for the claimant to bring its claim,

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funding costs are recoverable as part of the costs for the conduct of the arbitration. In the recent decision Essar Oilfield Services Ltd v Norscot Rig Management Pvt Ltd\textsuperscript{297} before the English High Court, the applicant applied to set aside an arbitration award on costs in which the respondent was awarded the costs of third-party funding. The arbitrator had ordered the applicant to pay costs on an indemnity basis, including a substantial amount which the respondent had paid to a third-party funder. The arbitrator held that the concept of costs was not merely limited to legal costs, but extended to any other reasonable costs incurred by parties, including funding costs. The arbitrator held that the applicant had deliberately put the respondent in a position where it could not fund the arbitration out of its own resources and it was therefore reasonable for the respondent to obtain funding from a third party on terms that if it succeeded it would pay the usual market standards for funding costs, namely 300\% of the amount advanced or 35\% of the amount recovered. The applicant challenged the decision of the arbitrator on the basis that the terms “other costs of the parties” (under s.59(1)(c) of the 1996 Arbitration Act\textsuperscript{298}) and “recoverable costs of the arbitration” (under s.63(3) of the 1996 Arbitration Act\textsuperscript{299}) do not include the costs of funding of the arbitration. The English court refused the application, holding that it was within the arbitrator’s discretion to construe the phrase “other costs” in s.59(1)(c) and “costs of the arbitration” in s.63(3) of the 1996 Arbitration Act as including costs of funding.\textsuperscript{300} The court stated that the correct approach was to take a functional approach to the term “other costs” and “costs of the arbitration”, and consider what other costs were incurred in bringing or defending the claim. The court noted that as a matter of language, context and logic “other costs” could include third-party funding costs.\textsuperscript{301}

The decision of the English courts in Essar has attracted considerable attention. Eventually, however, the Essar ruling should be treated as English authority for arbitrations seated in London under the English Arbitration Act and the English “indemnity rule”.

\textsuperscript{297} Essar Oilfield Services Ltd v Norscot Rig Management Pvt Ltd, Queen's Bench Division (Commercial Court) 15 September 2016, [2016] EWHC 2361 (Comm).

\textsuperscript{298} s.59 of the English Arbitration Act (1996) provides as follows: “59.— Costs of the arbitration.
(1) References in this Part to the costs of the arbitration are to—
(a) the arbitrators' fees and expenses,
(b) the fees and expenses of any arbitral institution concerned, and
(c) the legal or other costs of the parties.
(2) Any such reference includes the costs of or incidental to any proceedings to determine the amount of the recoverable costs of the arbitration (see section 63).”

\textsuperscript{299} s. 63 of the English Arbitration Act (1996) provides as follows:
“(1) The parties are free to agree what costs of the arbitration are recoverable;
(2) If there is no such agreement, the following provisions apply;
(3) ‘The tribunal may determine by an Award the recoverable costs of the arbitration on such basis as it thinks fit. If it does so, it shall specify—
(a) the basis on which it has acted, and
(b) the items of recoverable costs and the amount referable to each’.”

\textsuperscript{300} Essar Oilfield Services Ltd v Norscot Rig Management Pvt Ltd, Queen's Bench Division (Commercial Court) 15 September 2016, [2016] EWHC 2361 (Comm), paras 68-69.

\textsuperscript{301} Ibid, paras 56 and 68.
While it is accepted that arbitration costs may, in principle, include funding costs, it is suggested that funding costs, including success fees, should ordinarily not be recoverable. Most commentators agree that awarding funding costs as part of arbitration costs would substantially and unfairly increase the amounts owed by the losing party. A success fee payment to a funder results from a trade-off between the party and the funder and it is unreasonable for the respondent to be asked to pay the costs of a contract to which it is not a party. For these reasons, it is suggested that success fees or other premiums not be included in cost awards.

In arbitrations conducted under the English Arbitration Act the funded party may recover the third-party funder’s success fee under exceptional circumstances. This would be the case, for example, where the tribunal is satisfied that the conduct of the losing party was sufficiently egregious to warrant an award of costs (as was the case in Essar, where costs were awarded on the indemnity principle).

In the absence of exceptional circumstances involving egregious conduct of the losing party, third-party funder’s success fees might be recoverable only if the tribunal is satisfied that the funding cost has been incurred specifically to pursue the arbitration and only to the extent that the funding cost is reasonable, which should prevent recovery of success fees as high as 300% of the legal costs. By way of comparison, lawyers’ success fees in the context of conditional or contingency fee arrangements are typically capped in a number of jurisdictions. In Australia and in England, for example lawyers’ success fees are capped at 25-40%.  

In all cases, the requirement that costs must be reasonable provides the necessary assurances that the parties will be treated fairly and equally in terms of costs and that third-party funders will not enjoy unwarranted windfalls. Indeed, tribunals have occasionally dealt with similar issues on the basis of reasonableness, and have either included the funders’ return in the allocation of costs or not depending on their assessment of the case as a whole.


306 Compare Adem Dogan v. Turkmenistan, (ICSID Case No. ARB/09/9), Award (12 August 2014) not public, reported by Peterson, IA Reporter (19 August 2014) (where the tribunal awarded the claimant two thirds of
While the above analysis primarily refers to non-recourse funding costs, recourse based funding costs should not ordinarily be recoverable either. Indeed, ATE premiums are generally considered irrecoverable in arbitral proceedings.\textsuperscript{307} In the context of English litigation, the Jackson report, which approved third-party funding, considered that recoverability of ATE premiums led to disproportionate costs in civil litigation in England, and from April 2013, such costs are no longer recoverable in English litigation.\textsuperscript{308} There is no justification that ATE premiums should be recoverable as “reasonable costs” for an arbitration claim, not least because ATE does not fund the claim; rather it is there to meet any adverse costs.

As regards P&I and FD&D Clubs and other forms of mutual insurance, “calls” (i.e. premiums) are offered, usually annually, by members in advance of the dispute and are paid even if a dispute never arises for one of the members for the duration of the call. Thus, it would be difficult to classify them as “necessary” costs for arbitration even under the broader meaning of the term, given by English courts in the \textit{Essar} case. This may explain why there is no reported case awarding a party funded by a P&I and FD&D club its membership call as part of costs.

The same should apply to conditional or contingency fee arrangements (so that the uplift or success fee beyond the fees for the law firm’s time spent should not be recovered) as it essentially constitute funding of a party’s participation in arbitration by a law firm. As noted above, recoverability of lawyers’ success fees is typically capped in a number of jurisdictions.\textsuperscript{309}

\textbf{[3] Can arbitral tribunals render costs orders directly against third-party funders?}

\textsuperscript{307} Marie BERARD, ‘‘Other Costs’ in International Arbitration” in Cesar BETANCOURT (ed) \textit{Defining Issues in International Arbitration} (OUP 2016) 27.35 et seq.
\textsuperscript{309} See, e.g., \textit{City of Burlington v. Dague}, Supreme Court of the United States, Judgement of 24 April 1992, 505 U.S. 557 (only reasonable hourly fees recoverable instead of contingency fees); British Courts and Legal Services Act (1990), Section 58A(6) (as changed by virtue of section 44(4) Legal Aid, Sentencing and Punishment of Offenders Act 2012) provides that ‘[a] costs order made in proceedings may not include provision requiring the payment by one party of all or part of a success fee payable by another party under a conditional fee agreement’.
As regards the question whether a third-party funder may be ordered to pay adverse costs should the funded claim fail, state courts in England\(^{310}\) and the United States\(^{311}\) have ruled, in the context of litigation funding, that costs can be awarded against third-party funders if they have obtained a sufficient degree of economic interest and control in relation to the claim. In the context of litigation funding courts have emphasised that the third-party funders seek to gain financially from claims in as much as the funded parties and that “the derivative nature of a commercial funder’s involvement should ordinarily lead to his being required to contribute to the costs” on the same basis as the funded claimant.\(^{312}\)

The rationale behind these cases is simple: a funder who benefits financially if the client wins should not be able to walk away without any responsibility for adverse costs if the client loses. The important question, however, is whether the considerations underlying these cases can be transferred into the framework of international arbitral procedures.

Unlike state courts, which may be endowed with the power to order third parties to bear procedural costs by virtue of statutory procedural law, arbitral tribunals will typically lack jurisdiction to issue a costs order against a third-party funder because of the consensual nature of arbitration. The third-party funder is not normally party to the arbitration agreement, and has no involvement in the underlying dispute between the two parties in arbitration.\(^{313}\) While a number of non-signatory theories have been relied upon by national courts and arbitral tribunals to find that a non-signatory party is bound by an arbitration agreement, most of these theories will not apply to a typical third-party funding scenario. It would be difficult to envisage, for example, factual circumstances under which a third-party funder might qualify as the third party beneficiary, or an assignee or a principal, or the alter ego of the funded party, given the typical one-off and arm’s length commercial relationship and the lack of corporate links between a third-party funder and a funded party. Equally, while (depending on the factual circumstances) funders might be

\(^{310}\) Excalibur Ventures LLC v. Tex Kestone Inc. & Ors v. Psari Holdings Limited & Ors, English High Court (Queen’s Bench, Commercial Court), (Case No. 2010 Folio 1517), Order of 23 October 2014, [2014] EWCH 3436, paras 4, 161 confirmed by the Court of Appeal in Excalibur Ventures LLC v Texas Keystone Inc & Ors [2016] EWCA Civ 1144.; Arkin v. Borchard Lines Ltd. & Ors, English Court of Appeal, Judgement of 16 May 2005, [2005] EWCA Civ. 655 (“[w]here… the non-party not merely funds the proceedings but substantially also controls or at any rate is to benefit from them, justice will ordinarily require that, if the proceedings fail, he will pay the successful party’s costs”). See also the most recent case about a non-party costs order against insurers Legg and others v Sterte Garage Ltd and another [2016] EWCA Civ 97, where the Court of Appeal held that a costs order against the insurers was warranted because “(1) the insurers determined that the claim would be fought; (2) the insurers funded the defence of the claim; (3) the insurers had the conduct of the litigation; (4) the insurers fought the claim exclusively to defend their own interests; (5) the defence failed in its entirety.”

\(^{311}\) Abu-Ghazaleh v. Chaul, Florida Third District Court of Appeal, (Nos. 3D07–3128, 3D07–3130) Decision of 2 December 2009, 36 So. 3d 691.

\(^{312}\) Excalibur Ventures LLC v Texas Keystone Inc & Ors [2016] EWCA Civ 1144.

\(^{313}\) Compare Stavros BREKOULAKIS, Third Parties in International Commercial Arbitration (OUP 2010) paras 1.76-1.84.
involved (occasionally actively) in the arbitration proceedings, this will not usually be sufficient
to establish implied consent to the arbitration agreement by conduct. The test for treating a non-
signatory as a party in arbitration is demanding, and courts, particularly in common law
jurisdictions, have noted that it is the signatories on the face of an agreement who should normally
be considered as the parties in an arbitration.

Notwithstanding the above, it is worth noting that the 2017 SIAC Investment Arbitration
Rules provide in Article 35 that “The Tribunal shall have the authority to order in its Award that
all or a part of the legal or other costs of a Party be paid by another Party. The Tribunal may take
into account any third-party funding arrangements in ordering in its Award that all or a part of
the legal or other costs of a Party be paid by another Party.” Eventually, whether such a cost award
would be enforceable against a third party in an arbitration should depend on the national law of
the place of enforcement, although as discussed above non-signatories, including third-party
funders, are difficult to be held bound by an arbitration agreement or an arbitration award under
most national laws.

In policy terms, there are conflicting considerations. While on the one hand there is an
argument to the effect that a funder who benefits financially (if the funded party is successful)
should not be able to escape responsibility for adverse costs if the funded party loses, on the other
hand, a funder will lose its investment if the funded party loses its cases. Ultimately, any policy
considerations are not sufficient to amend fundamental principles of consent underpinning the idea
of arbitration. A lesser degree of (costs) control over third parties is a typical feature of arbitration
and must arguably be accepted if one chooses arbitration over litigation.

The position does not differ in the case of recourse based funding. Both ATE insurers and
P&I and FD&D clubs will typically assume the contractual obligation to pay adverse costs,
although such contractual obligation is vis-à-vis the insured, i.e. the funded party. The level of
control of BTE and ATE insurers over the claim differs. For example, a FD&D club will typically
exert a high degree of control over the claim as is often permitted by its rules. Whether such control
can allow tribunals in practice to decide that a FD&D club has effectively become a proper party
to the arbitration on the basis of any of the known non-signatory theories will depend on the factual
circumstances of the case. In the context of English litigation, and for comparative purposes, the
Court of Appeal held in the recent Legg and others v Sterte Garage Ltd and another [2016] EWCA

314 See Jonas VON GOELER, Third-Party Funding in International Arbitration and Its Impact on Procedure
315 See for example, the decisions of the English Supreme Court in Dallah v Government of Pakistan, [2010]
UKSC 46, and the decision of the English High Court in Peterson Farms Inc v C&M Farming Ltd [2004] 1 Lloyd’s
Rep 603, the decision of the Court of Singapore in PT First Media TBK v Astro Nusantara International BV and others
[2013] SGCA 57, the decision of the Swiss Federal Tribunal, Decision 4A_450/2013 on 7 April 2014.
Civ 97, that a costs award against a third party insurer that first ran the case and then withdrew support was warranted. While the level of control by the funder in this case was significant, the difference with arbitration is the compulsory jurisdiction enjoyed by the court as to opposed to the arbitration tribunal’s reliance on consent.
2. Security for Costs

Like any party, where a funded party is unsuccessful, it may be unable to comply with any costs award rendered against it, especially if it is impecunious. If there is evidence that the existence of a funding agreement may impact on the non-funded party’s ability to recover costs, that party (typically the respondent) can apply to a tribunal for interim or conservatory measures to ensure that any costs awarded against the claimant will be complied with. In those circumstances, an arbitral tribunal must balance the claimant’s interest in having access to arbitral justice and the respondent’s interests to recover costs if it wins. Both in commercial and investment arbitrations, arbitral tribunals will typically have the power to order security for costs either pursuant to arbitration laws and rules which explicitly provide for such power or general provisions on interim measures which, as is generally accepted, include security for costs orders. Assuming that an arbitral tribunal will shift costs to the losing party (see previous section), the question arises as to how third-party funding arrangements may affect whether an arbitral tribunal should grant security for these – potentially recoverable – costs. Two questions arise here: the first is whether tribunals do have the power to award security for costs. The second is whether they should award security for costs when the claimant is funded by a third party.

A. Whether Tribunals Have the Power to Award Security for Costs

As regards an arbitral tribunal’s power to order security for costs, three situations can broadly be identified. No problems should arise where the parties have expressly conferred to the tribunal the power to order security for costs, or have agreed to arbitrate under an arbitration law that expressly allows arbitrators to order security for costs, or have chosen arbitral rules containing such provisions. The situation is less clear where the applicable arbitration law or arbitration rules only contain a general clause providing for interim measures. Recently, an ICSID tribunal noted that one of the reasons why the general clause on interim measures contained in Article 47 ICSID Convention should cover security for costs is that, when the ICSID Convention was drafted in 1965, ‘issues such as third party funding and thus the shifting of the financial risk

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316 See, e.g., English Arbitration Act (1996), s. 38(3); LCIA Rules (2014), Art. 25(2).
318 See, e.g., English Arbitration Act (1996), s. 38(3); Hong Kong Arbitration Ordinance (2011), s. 56(1)(a).
away from the claiming party were not as frequent, if at all, as they are today’. In the third situation, neither express provisions nor a general clause on interim measures exists that could serve as a basis for the tribunal’s power to order security for costs. In that case, it can still be argued that the tribunal’s power to order security for costs is anchored in its inherent power to preserve the integrity of the proceedings, albeit in such a case the respondent may have to prove the requirements for interim relief set out by the applicable national law, which often include necessity and urgency and no prejudgment.

B. Whether Tribunals should Award Security for Costs when the Claimant is Funded by a Third Party

While tribunals normally apply different tests depending on whether the case is an investment or commercial arbitration, the common, and ultimate, consideration is the evaluation of the claimant’s financial situation. The following sections provide an overview of the tests and considerations under both investment and commercial arbitration. The analysis concludes with general observations applying to both types of arbitration.

1. Investment Arbitration

[a] Do states have a protected right to security for costs under ICSID arbitration?

While the ICSID Convention provides that each party must abide by and comply with the terms of the award, execution of the award is left to the national applicable law. Accordingly, because the ICSID Convention is not concerned with execution or collection of awards, including the collection of a possible costs award, some tribunals and arbitrators have questioned whether a defendant State has a “right” to security for costs which is protected under the ICSID regime. In Maffezini v Spain for example, the tribunal noted that there was no present rights of the respondent

321 RSM Production Corporation v. Saint Lucia, (ICSID Case No. ARB/12/10) Decision on Saint Lucia’s Request for Security for Costs (13 August 2014) para. 55. Whether the explanation offered by the Tribunal in this case is accurate or supported by the history of drafting the ICSID Convention is questionable, and the question of the propriety and jurisdiction to order a State to post security for costs is much more complex.

322 Laurence CRAIG, William PARK and Jan PAULSSON, International Chamber of Commerce Arbitration, 3rd edn (OUP 2000) p. 467 (who report that even when the ICC Rules did not yet contain a general clause for granting interim measures, ‘ICC tribunals had found that they had the power to grant security for costs as part of their inherent powers in connection with the conduct of arbitral proceedings’) (with further references); Commerce Group Corp. & San Sebastian Gold Mines, Inc. v the Republic of El Salvador, (ICSID Case No. ARB/09/17), Annulment Proceeding, Decision on El Salvador’s Application for Security for Costs, (20 September 2012), para. 45.


324 ICSID Article 53(1).

325 ICSID Article 54(3).
State to be preserved. In Grynberg v Grenada, the dissenting arbitrator stated that “the use of the words ‘preserve’ and ‘preserved’ in [ICSID] Article 47 and Rule 39 presupposes that the right to be preserved exists. Because Respondent has no existing right to an ultimate award of costs, the Tribunal is thus without jurisdiction”.

Other ICSID tribunals, such as the tribunal in EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic and the majority decision in Grynberg v Grenada, accepted that States have a right in a security for costs application, which is protected under the ICSID regime, even if under the circumstances of the case tribunals refused to grant States the requested security for costs.

In this regard, the tribunal in the recent, Eskosol S.P.A. in Liquidazione v Italian Republic, noted that “there is something analytically curious about the notion that an ICSID tribunal, while not empowered to protect a claimant’s ability to collect on a possible merits award, nonetheless should intervene to protect a State’s asserted “right” to collect on a possible costs award”. While the tribunal in the Eskosol case decided not to address this matter as the respondent had failed to demonstrate that the security for costs request was urgent even assuming that the State had a protectable right, it went on to observe that:

“The Tribunal accepts that respondent States have genuine concerns about their ability to enforce an eventual costs award against unsuccessful claimants, and some States are starting to raise the possibility of reforms to the ICSID system to protect themselves more systematically. But at the same time, such States would be unhappy to see a similar argument about a right to effective relief used against them, for example by claimants worried about collection risk associated with any final merits award of compensation.”

Ultimately, this is still an emerging matter, which is included here for the sake of completion. The Task Force does not wish to take a position on this matter at this stage.

[b] Additional Criteria

From a review of a growing number of cases dealing with this matter, it is clear that tribunals in ICSID arbitration tend to adopt a stricter test than the claimant’s impecuniosity to order security for costs: they usually require evidence of abusive conduct or bad faith on the part of the

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326 Emilio Agustín Maffezini v. Kingdom of Spain, (ICSID Case No. ARB/97/7) Procedural Order No. 2 (28 October 1999), para. 15.
327 Rachel S. Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg and RSM Production Company v. Grenada, (ICSID Case No. ARB/10/6), Tribunal’s Decision on Respondent’s Application for Security for Costs (14 October 2010), para. 5.16, in fn. 9.
328 EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic, (ICSID Case No. ARB/14/14), Procedural Order No. 3 (23 June 2015).
329 Eskosol S.P.A. in Liquidazione v Italian Republic, (ICSID Case No. ARB/15/50) Procedural Order No. 3 (Decision on Respondent’s Request for Provisional Measures), (12 June 2017) para. 35.
330 Ibid., para. 34.
claimant,\textsuperscript{331} such as evidence that the claimant has a track record of deliberately failing to comply with costs awards.

While this appears to be an increasingly accepted test for investment arbitration tribunals, it is questionable whether such high threshold is warranted. It can reasonably be argued that, if the respondent state was subject to an unsuccessful claim, it should be able to recover costs at the end of the arbitration regardless of whether the claimant is acting in bad faith or not.

On the other hand, an investor may claim that it would be unreasonable for a tribunal to order an investor to meet a security for costs order, because the state’s unlawful conduct (assuming that the state’s conduct in question is indeed unlawful) has diminished or even expropriated their investment in the first place, and have left the investor with limited or no available funds to conduct a usually costly investor-state arbitration. This can be a powerful claim, not least because it raises obvious issues of access to justice for the investors.

In practice however, when investor-state tribunals decide, usually at an early stage of the arbitration process, security for costs requests they tend not to accept an assumption that the state’s conduct has indeed left an investor with limited available funds to avoid prejudging the merits of the dispute and thus violating fundamental principles of procedural fairness.

This explains why investment tribunals tend to focus on other considerations, which are not directly related to the merits of the dispute, but nevertheless set a high threshold for a claimant to be subject to a security for costs order in investment arbitration, including for example the requirement that the claimant has exhibited abusive conduct by repeatedly failing to comply with costs orders or deliberately dissipating its assets.

Against this background, it is perhaps unsurprising that investment arbitration tribunals have consistently dismissed applications for security for costs in the past. In doing so, these tribunals have relied on a range of different arguments, such as the following:

\begin{itemize}
\item improper to prejudge the claimant’s case;\textsuperscript{332}
\item failure to establish concrete risk of non-payment;\textsuperscript{333}
\end{itemize}


\textsuperscript{333} \textit{Victor Pey Casado and President Allende Foundation v. Republic of Chile}, (ICSID Case No. ARB/98/2), Decision on Provisional Measures (25 September 2001), para. 89; \textit{Burini S.R.L. and Eagle Games SH.A. v. Republic of Albania}, (ICSID Case No. ARB/11/18), Procedural Order No. 2 (3 May 2012), para. 39; \textit{Alasdair Ross Anderson et al. v. Republic of Costa Rica}, (ICSID Case No. ARB(AF)/07/3), Award (19 May 2010), para. 9; \textit{Abaclat and others v. The Argentine Republic}, (ICSID Case No. ARB/07/5), Procedural Order No. 10 (18 June 2012); \textit{Rachel S. Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg and RSM Production Company v. Grenada}, (ICSID Case No. ARB/10/6) Tribunal’s Decision on Respondent’s Application for Security for Costs (14 October 2010), para. 5.21; \textit{Libananco
• not unusual that the claimant is a vehicle or has no assets; \(^{334}\)
• would limit claimant’s access to justice; \(^{335}\)
• no threat to the integrity of the proceedings. \(^{336}\)

[c] Third-Party Funding as Abuse or Bad Faith?

If we assume that the test in investment arbitration is thus that the respondent must demonstrate exceptional circumstances in the form of an element of bad faith or abuse on the claimant side, what does a claimant’s recourse to third-party funding indicate in this respect?

Some have argued that third-party funding should in itself be a reason for ordering security against the funded party, or at least shift the burden of proof to the effect that the funded party must make a case why security should not be granted. \(^{337}\) Another point frequently raised by respondents in order to demonstrate an element of bad faith is that recourse to funding would result in situations where the claimant’s expenses are being covered by a related entity or individual who stands to gain if the claimant wins, but would not be liable to meet any award of costs that might be made against the claimant if it lost.

The growing body of arbitral case law on this question, however, provides a clear picture: mere recourse to third-party funding does not carry an element of bad faith or abuse; the existence of a funding agreement alone is not sufficient to grant security for costs.

The first case to explicitly address the issue was *RSM Production Corporation v. St Lucia*, where an ICSID tribunal – for the first time ever in investment treaty arbitration – issued a security for costs order. \(^{338}\) The respondent argued that, while no ICSID tribunal had ordered security

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\(^{337}\) See notably *RSM Production Corporation v. Saint Lucia*, (ICSID Case No. ARB/12/10), Assenting Reasons of Gavan Griffith (12 August 2014).

before, such measure would be justified here, pointing out that the claimant had failed to pay ICSID’s advance on costs, had not honoured costs awards rendered against it in a number of previous ICSID arbitrations, and that “the proceedings initiated by Claimant are funded by third parties”. Claimant’s counsel had admitted this already at a hearing on ICSID’s advance on costs.

The respondent further claimed that these third parties would not be liable for adverse costs, enabling the claimant to engage in “arbitral hit and run”. The claimant contested the tribunal’s jurisdiction to order security and additionally argued that a difficult financial situation would not be sufficient to grant security payment against claimants in ICSID proceedings. It moreover stated that its current conduct would not give reason to doubt its willingness to pay adverse costs. In reaching its decision to order security payment, the RSM tribunal did take into account that the claimant was impecunious and was funded by a third-party that could presumably not be made responsible for any adverse costs award. Notably, the tribunal pointed out that it would be “unjustified to burden Respondent with the risk emanating from the uncertainty as to whether or not the unknown third party will be willing to comply with a potential cost award”. Yet, the decisive factor for the tribunal to grant the requested security for costs was the fact that the claimant had a proven history of not complying with costs awards rendered against it, and that the third-party funder was not revealed (and was therefore unknown) to the tribunal.339

In another decision on the matter, EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic,340 the respondent advanced strikingly similar arguments, arguing not only that it had a good case on the merits, but also that the claimants “have a history of engaging in fraud and reneging on payment obligations’ and that they do not have the means to pay for the costs of the arbitration proceedings, which are entirely funded by third parties”. The claimants contested the tribunal’s power to order security for costs, argued that ordering security would unduly restrict their access to justice, and that their financial difficulties are “in large part attributable to acts and omissions of Respondent”. The arbitrators explicitly distinguished the case before them from RSM Production Corporation v. Saint Lucia and denied the respondent’s security request, pointing out that “the underlying facts in [the RSM] arbitration were rather exceptional since the claimant was not only impecunious and funded by a third party, but also had a proven history of not complying with cost orders. As underlined by the arbitral tribunal, these circumstances were considered cumulatively.” The tribunal went on to note that the respondent had failed to establish that the claimants had defaulted on their payment obligations in the present proceedings or in other arbitration proceedings. It concluded by making it clear that “financial difficulties and third-party funding – which has become a common practice – do not necessarily constitute per se exceptional circumstances justifying that the Respondent be granted an order of security for costs.”

In South American Silver Limited v. The Plurinational State of Bolivia, the respondent argued that the claimant was an impecunious shell company which was funded by a third party, which in combination, according to some arbitrators, would create “a prima facie case for granting

339 Ibid, para. 86.
340 EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic, (ICSID Case No. ARB/14/14), Procedural Order No. 3 (23 June 2015).
the cautio judicatum solvi”, meaning that the burden of proof is transferred to the funded party, who must prove why the cautio judicatum solvi should not be ordered. 341 Referring to RSM v. St. Lucia, the claimant pointed out that “the only investment tribunal that has ever issued security for costs did so primarily because of the claimant’s notorious history of failing to pay prior cost awards”, and that the position that “the mere uncertainty as to the existence of a third-party funder’s obligation to reimburse constitutes ‘compelling grounds for security for costs’ correspond[s] to a minority view”, while “[t]he majority of international tribunals have stated the contrary in recent decisions, and on the contrary, the existence of a funder indicates that the claim is plausible on the merits”. The PCA tribunal transferred the “extreme and exceptional circumstances-test” favoured by ICSID tribunals into the framework of Article 26 of the applicable UNCITRAL Arbitration Rules, concluding that “Bolivia’s mere analysis of SAS’ or SASC’s balances and other related accounting documents, or the mere existence of a third-party funder do not meet the high threshold set forth by investment tribunals.” 342 In reaching this conclusion, the tribunal explicitly referred to the two previously mentioned cases, and confirmed that “the mere existence of a third-party funder is not an exceptional situation justifying security for costs”, explaining that:

“[i]f the existence of these third-parties alone, without considering other factors, becomes determinative on granting or rejecting a request for security for costs, respondents could request and obtain the security on a systematic basis, increasing the risk of blocking potentially legitimate claims.” 343

In a procedural order issued in April 2017 in the case Eskosol S.P.A. in Liquidazione v Italian Republic, 344 the tribunal rejected the respondent’s request for an order that the claimant post a bank guarantee of US $ 250,000 or prove it had obtained an undertaking from its third-party funder to pay any costs awards against it, notwithstanding the fact that the claimant had been declared insolvent and placed under receivership in 2013. In its security for costs application the respondent argued that the claimant’s insolvency made it unlikely that it would be able to meet any adverse costs, if the claim was declined. The respondent further argued that a security for costs order was necessary and urgent because it had “a suspicion” that the claimant was funded by a third-party funder, which –according to the respondent- increased the risk that the claimant would not comply with a costs order. Responding to the security for costs application, the claimant confirmed that it had been funded by a third-party funder which had assisted the claimant to purchase an ATE insurance policy protecting the company against adverse costs of up to Euros 1 million. While accepting that the claimant’s insolvency meant that the claimant would be unable

343 Ibid., para. 77.
344 Eskosol S.P.A. in Liquidazione v Italian Republic, (ICSID Case No. ARB/15/50) Procedural Order No. 3 (Decision on Respondent’s Request for Provisional Measures), (12 June 2017). See also above p.118.
to meet an adverse costs award from its own funds, the tribunal stated that the ATE insurance policy was sufficient to cover the amount of costs requested by the respondent. The tribunal thus concluded that the respondent had failed to demonstrate that it is either necessary or urgent to grant the security for costs application.

However, in two recent procedural orders issued in July 2017 in relation to the same investment dispute in the parallel cases of Luis Garcia Armas v Venezuela and Manuel Garcia Armas et al. v Venezuela, the tribunal (sitting on both cases) ordered the funded claimants to provide evidence on their solvency before deciding a request for security for costs made by the respondent State.

In the cases, the claimants had voluntarily disclosed the existence of a third-party funding agreement. In response to a request by the respondent State, the tribunal had subsequently ordered the claimants to disclose the actual terms of their funding arrangements. Because the funding agreement included a provision that the funder did not undertake to finance any adverse costs related to the arbitration, the respondent requested that the tribunal order the claimants to post a US$5 million bond as security for adverse costs.

Before deciding on the request for security, the tribunal asked the claimants to provide reliable evidence of their solvency, including asset valuations. The claimants were also directed to inform the tribunal of the jurisdiction(s) where those assets were located, in order to assess the enforceability of any future adverse costs order. These proceedings are still ongoing and the decision on the respondent’s security for costs application is still pending, but the tribunal’s request that the claimants provide evidence of their solvency appears to have shifted the burden of proof of impecuniosity from the respondent to the claimants.

3. Commercial Arbitration

[a] Additional Criteria

In international commercial arbitration, no uniform test for security for costs applications exists at this point. One approach is to ask whether the prospect of the claimant honouring a potential adverse costs award has substantially and unforeseeably deteriorated since the conclusion of the arbitration agreement. The idea here is to take into account that the parties to an international commercial arbitration have agreed to arbitrate, which can be taken as a reference point in determining a party’s legitimate expectations in recovering costs. For instance, a respondent that has agreed to arbitrate with a claimant that was in financial distress at the time the

345 Luis Garcia Armas v Venezuela and Manuel Garcia Armas et al. v Venezuela, (ICSID AF Case No. ARB(AF)/16/1) Procedural Order (7 July 2017) administered by ICSID’s Additional Facility Rules; PCA Case No. 2016-08, administered by the Permanent Court of Arbitration, (Both with the seat in The Hague, The Netherlands).

arbitration agreement was signed should expect that, if a dispute arises, its counterparty may not be financially able to comply with an adverse costs award. Moreover, the possibility that the credit standing of a business partner changes over time is part of normal commercial risk, in other words, cannot readily be characterized as commercially unforeseeable.

Another approach would be to apply a broader fairness test, i.e. requiring “that the present situation is of such a nature as to render it highly unfair to require it to conduct the arbitration proceedings without the benefit of such security.”347 This perspective allows arbitrators to capture the nuances of the particular case, but, on its own, may be considered excessively vague and open-ended.

[b] Application to Third-Party Funding Scenarios

[aa] Conclusion of Funding Agreement as Material Change of Circumstances?

When deciding security for costs applications, the majority of commercial tribunals adopt a consent-based approach, looking into whether a material and unforeseeable change of circumstances has occurred since the conclusion of the arbitration agreement. In this regard, the relevant question is whether the conclusion of a funding agreement constitutes such material and unforeseeable change of circumstances.

There is an argument to the effect that the existence of third-party funding is relevant to an application for security for costs, as it implies that the funded party is impecunious per se. Further, there have been cases where arbitral tribunals have found that the entering into of an arbitration funding agreement did constitute ‘a fundamental change of circumstances which would justify granting security for costs’.348

On the other hand, however, there is rising concern that non-funded parties are using the “impecuniousness assumption” to justify routinely submitting security applications as a means of delaying and deliberately increasing the costs of the resolution of meritorious claims.

Obtaining funding from a third party should not be taken to suggest material deterioration of the claimant’s finances, since funding is widely used by financially stable parties in order to share risk and maintain liquidity.

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348 Although the tribunal in this case seems to have applied a broader fairness test (see discussion under [bb]): X v. Y and Z, (ICC Case) Procedural Order (3 August 2012), published in Philippe PINOLLE, “Third Party Funding and Security for Costs” Cahiers de l’arbitrage/Paris J. Int’l Arb. 399, 2013(2), paras 28, 33. See also discussion above in p. 71.
Broader Fairness Concerns

The situation looks quite different if one applies a broader fairness test to third-party funding scenarios, which is essentially what an ICC tribunal did in an order dated 3 August 2012. The terms of the funding agreement were on the record because claimant’s counsel had previously transferred the agreement to the respondent, without indicating any reasons for this. The tribunal therefore examined in great detail the terms of the funding agreement and ultimately granted the security order, essentially because (1) the claimant was a holding company based in Cyprus that was unlikely to be able to pay adverse costs; (2) the funding agreement did not cover adverse costs; and (3) in the tribunal’s view the funder’s termination rights under the funding agreement meant that the funder was “empowered to terminate the Agreement at any time, entirely at its discretion”.

The tribunal pointed out that the claimant engaged in an unfair “cherry-picking”: the funding agreement enabled the claimant to arbitrate as if it was solvent while not assuming the economic risk of this arbitration due to its impecuniosity. In addition, according to the reading of the arbitrators, there was a risk of the funder walking out at any time, leaving the claimant without means to continue with the arbitration or pay adverse costs. Some may even want to go a step further and argue that the asymmetric situation of a claimant being able to arbitrate while not running economic risks as to the arbitration is in itself sufficient to grant security for costs. Certainly, there are valid counter-arguments: the claimant here was impecunious from the start, so that the respondent could never really expect to have security to recover its costs. If a tribunal indeed wishes to take into account broader fairness considerations and ask whether it would be unfair for the funded party to proceed without security in light of all circumstances, this will require an analysis of the precise terms of the funding agreement, which might in turn be used as an argument in favour of disclosure of such agreement. Another important aspect for arbitrators to be aware of and take into account are arrangements between the funder and the funded party as to whether the former has undertaken to finance any adverse costs. Where the funder is liable to the funded party to cover an adverse costs order and the capital adequacy of the funder to meet an adverse costs award is shown, an order for security for costs may be seen as dispensable.

While looking into broader fairness considerations is an interesting approach, it clearly remains a minority one, with tribunals in commercial arbitration normally adopting a consent-based view on security for costs applications and applying a “material of change of circumstances” test.

350 No other case than the ICC X v. Y and Z, (ICC Case), Procedural Order (3 August 2012), referred to above has been reported taking a broader fairness approach.
3. Concluding analysis for both investment and commercial arbitration

A key aspect in any security for costs analysis will be the financial situation of the party against which security payment is requested. There must be sufficient evidence to conclude that the current financial circumstances of the claimant are such that it will not be able to pay the respondent’s costs at the end of the proceedings.

What, then, is the relevance of a third-party funding agreement in determining whether the claimant is impecunious? On the one hand, it could be argued that the fact that a claimant is actively seeking external funding to pursue its claim is evidence (or at least an indication) of the claimant’s difficult financial circumstances. It might even be said that the existence of third-party funding arrangements should set a rebuttable presumption for the claimant’s impecuniosity. However, the assumption that a funded Party is impecunious miscomprehends the current state of third-party funding. Most of the funders, including in the Task Force, suggest and arbitration practitioners confirm that third-party funding is increasingly used by large, solvent companies that simply wish to share risk and maintain liquidity. As it has been pointed out, “companies that want to maintain sufficient cash flow to continue their regular business while the arbitral proceedings are ongoing, or that simply want to share the risk of the arbitration with a third party” may “seek financing to pursue a meritorious claim.” As has been noted “third-party financing is increasingly a tool of choice, not of necessity. Some of the world’s largest companies are regular users of outside financing.”

It is thus suggested that applications for security for costs in international arbitration should be determined irrespective of any funding arrangement, and on the basis of impecuniousness. In the first instance, the burden should be on the moving party, and it is suggested that no party should have to defend a motion for security unless and until the moving party makes a prima facie showing of impecuniousness. If no such showing is made, then the motion should be denied outright.

If a party is found to be impecunious, that party should then be given the opportunity to present additional evidence of funding or have a security for costs award imposed. If the party has third party arrangements in place, in which the funder agrees to pay any costs award, it could then be submitted to the tribunal as evidence that no security need be posted.

351 See for example, RSM Production Corporation v. Saint Lucia, (ICSID Case No. ARB/12/10), Assenting Reasons of Gavan Griffith, (12 August 2014).
At that stage, a request for disclosure of third-party funding agreements should normally be accepted as the moving party and the tribunal should be able to examine the relevant parts of the third-party funding agreement in the context of the security for costs application against an impecunious party. In this regard, ordering disclosure of the third-party funding agreements in their entirety may have a negative effect on the arbitration proceedings. Tribunals are thus encouraged to limit disclosure orders to the provisions that are strictly necessary to assess the extent to which the funder may cover (or not) an adverse costs order. Another approach could be to allow the funded party, its counsel or even the funder to provide the tribunal with an affidavit stating its identity and whether under the third funding party agreements it can be held liable for adverse costs.

One important provision in a third-party funding agreement, which the tribunals should review, will be the provision about whether the funder has agreed to cover adverse costs, including an order for security for costs. The funding agreement should normally clearly set out whether the funder will pay a defined sum to the claimant in the event of an adverse award of costs, whether that promise endures if the funding agreement has been breached or otherwise terminated, and whether the funder will pay any order of security for costs. And if the party is impecunious, both the funder and party should be aware that a funding agreement in which a funder is not obligated to irrevocably pay an award of costs may cause the tribunal to order security for costs. The recent Hong Kong Arbitration and Mediation (Third-Party Funding) (Amendment) Bill 2016 includes as an Annex a non-binding Code of Practice for third-party funders in arbitration which provides in s.2.14(3) that “the third party funding agreement must state whether (and if so to what extent) the third party funder, a subsidiary or an associated entity is liable to the funded party to provide security for costs”. In all cases, where a funder has agreed with the funded party to finance any adverse costs, the capital adequacy of that funder to meet an adverse costs award, whether in its own right or by virtue of an ATE policy, is clearly relevant in assessing whether adequate security has been provided.

Another relevant provision in the context of a security for costs application will be the provision in a third-party funding agreement about the funder’s termination rights. Where a third-party funder has agreed to finance adverse costs, whether and under which conditions a funder can discontinue funding may be a relevant consideration for tribunals to take into account. Most professional funders have very clear termination provisions which set out, in circumstances where they have agreed to be liable for adverse costs, when they are liable for such costs, which typically is for the duration of their funding. Where a funder is a member of the Association of Litigation Funders of England and Wales (ALF), its funding agreements must comply with the ALF Code of Conduct for Litigation Funders (ALF Code, January 2014). Article 13.2 ALF Code requires that, in case of a dispute over termination, ‘a binding opinion shall be obtained from a Queen’s Counsel who shall be instructed jointly or nominated by the Chairman of the Bar Council’. Only if the Queen’s Counsel agrees with the funder that it is lawful to terminate, will the Termination Notice be valid. Funders operating in other jurisdictions have internal codes that set out their practice in respect of whether and under which circumstances they can terminate funding. In all cases where
the defendant has previously knowingly proceeded on the basis that the funder would meet the
adverse costs, it is suggested that third-party funders or funded parties should notify the defendant
if funding is discontinued.

If a tribunal decides that a security for costs order is warranted, it can order security for
costs by way of a bank guarantee. That should be a sufficient form of assurance. By way of
comparison, in cases where the claimant is funded by a P&I and FD&D club or an ordinary insurer,
security for costs can be provided by way of a club letter of guarantee or an insurer’s bond. The
club and insurer have a contractual obligation to indemnify its member or insured for any liability
incurred, including costs award. For the same reasons, an ATE insurance policy should also be
considered adequate evidence that the claimant will meet an adverse costs award. Payment into a
bank account may be ordered for security for costs in exceptional circumstances, and where there
is no ATE or any other form of evidence of indemnification arrangements already in place.354

Finally, when a security for costs application is lodged, an arbitral tribunal should
consider indicating to the respondent (the requesting party) that, should the claimant prevails on
the merits of the case, the respondent will be held liable for the costs reasonably incurred by the
claimant (funded party) in posting security. It should be for the claimant (funded party) to
substantiate the amount of costs it reasonably incurred in posting security. This seems desirable
from a policy perspective, as it provides a legally fair and financially risk neutral solution to
granting security for costs. At the beginning of the proceedings, the tribunal can at best perform a
prima facie assessment of the respondent’s chances of succeeding on the merits. If the tribunal
denies the respondent’s application for security it risks evaluating the merits in a way that ex post
may prejudice the respondent, should the respondent ultimately prevails and be unable to recover
costs. At the same time, if the tribunal grants the respondent’s security request and the claimant
ultimately prevails, the security application would turn out to be a win-win option for the
respondent, as there would be no downside for having requested (as it turned out unnecessary)
security. By granting security payment on the premise that the respondent must contribute towards
the cost of the security should the claimant prevails on the merits, the tribunal can restore the
financial balance between the parties, both of which continue to run risks in relation to the money
posted. This avoids prejudging the case in favour of either side.

354 Unless of course the claimant offers to pay a cash deposit, if this is easier and cheaper than arranging for
a bank guarantee.
Chapter 7†

Best Practices in Third-Party Funding Arrangements

As noted in Chapter One, in its early work, the Task Force engaged in considerable debate about what form its final work product should take. Early suggestions ranged from drafting a code of conduct for third-party funders in international arbitration, similar to the Association of Litigation Funders Code of Conduct in England and Wales, to abstaining from producing any form of guidance. Against the backdrop of these discussions, the Task Force ultimately agreed on two general objectives for the Task Force’s work: (1) to promote greater understanding about what third-party funding is and the issues it raises in international arbitration; and (2) to facilitate greater consistency and more informed decision-making in addressing issues relating to third-party funding. In pursuing these objectives, the Task Force also decided to limited its work to those issues that: (1) directly affect international arbitration proceedings; and, (2) are capable of being addressed at an international level.

The issues addressed in the preceding chapters largely fulfil these objectives and limitations. Chapter Four addresses issues relating to disclosure and arbitrator conflicts of interest; Chapter Five addresses issues relating to privilege; and Chapter Six addresses issues relating to costs and security for costs.

While those chapters provide analysis of the issues they address, they do not address many more basic questions that parties and counsel new to third-party funding, and funders new to international arbitration, often have. Moreover, many of the principles in those chapters rely on certain fundamentals being effectively addressed either in the funding agreement or in the parties’ negotiations. For example, the principles regarding privilege in Chapter Five rely on, or at least are most effective when, the funder and the party have entered into a non-disclosure agreement.

This Chapter aims to fill that gap by providing further guidance in the form of articulation of what constitutes good and responsible practices in entering a funding arrangement, including a checklist for parties and counsel to consult. To that end, the Chapter proceeds as follows: it first provides some general background about funding in national legal systems [I]; it then collects the Principles articulated in other Chapters of this Report and articulates additional best practice norms [II], and finally provides a due diligence checklist that parties (and their counsel) can use as they consider entering into a funding agreement [III].

I. Background

Many common law jurisdictions have historically prohibited the funding of litigation (and other forms of dispute resolution) by parties other than those directly involved in the dispute. And some still do. Although such prohibitions have come in many forms over the years, in common law jurisdictions they usually appear as laws prohibiting maintenance and champerty. In plain terms, maintenance is the support of litigation by a stranger without just cause. Champerty, a form of maintenance, is the support of litigation by a stranger in return for a share of the proceeds.

In those jurisdictions where such laws still exist, third-party funding is prohibited. In Ireland, for example, maintenance and champerty are both criminal offences and civil torts, and have been since the 1600s. As recently as 2016, The High Court of Ireland held that third-party
litigation funding violated its maintenance and champerty laws. In the *Persona* decision, the High Court confirmed—consistent with a long line of authority—that the provision of financial assistance to support litigation by a third party in return for a share of the proceeds is both contrary to public policy and an abuse of process, unless that third party has a genuine interest in the litigation. Although an appeal has been accepted by the Supreme Court of Ireland, for now, third-party funding is prohibited in Ireland.

Other jurisdictions that historically prohibited third-party funding under maintenance and champerty laws have recently introduced reforms to expressly permit third-party funding in international arbitration. Notably, Hong Kong recently enacted legislative reforms to permit third-party funding arrangements that were previously prohibited. The new legislation expressly provides that the doctrines of maintenance and champerty do not apply to domestic or international arbitrations.³⁵⁶ The proposed amendments also establish certain disclosure obligations for funded parties, as well as ethical and other standards for counsel and third-party funders.

Singapore has also recently amended its laws to allow for third-party funding in arbitration. As in Hong Kong, the new Singapore law makes clear that the use of third-party funding in international arbitration is not prohibited by existing maintenance and champerty laws, nor is it contrary to public policy.³⁵⁷ The new law also provides certain disclosure obligations for funded parties and imposes certain regulations and financial standards on third-party funders.

The purpose of these Best Practices is not to identify the various legal permutations that may affect the ability of a party to obtain third-party funding in a particular jurisdiction. But parties should be aware that third-party funding remains prohibited in some jurisdictions and should generally seek the advice of local counsel before engaging a third-party funder.

The questions on this Checklist are designed to help parties, counsel, and third-party funders identify the kinds of questions should be considered when deciding whether to enter into third-party funding arrangement. In particular, this document seeks to identify the key questions that may assist a potential user of third-party funding in determining whether (i) the potential funder is financially able to fund the case in accordance with a state of the art funding agreement, (ii) the potential funder’s interests are compatible with those of the potential party, and (iii) the potential funder offers adequate assurances in relation to the integrity and conduct of the case.

The main purpose of the Checklist is to prompt consideration and inquiries that may assist in identifying important details for inclusion in a proposed funding agreement in order to reduce the likelihood of potential misunderstandings due to incompleteness and/or lack of clarity.

**II. Principles and Best Practices**

This Part of the Chapter collects [A.] the Principles provided for in other chapters, and articulates [B.] several Principles of Best Practices for consideration by parties, funders, counsel, and arbitrators.

³⁵⁷ See Civil Law (Amendment) Act 2017, §5(b)(2), available at <http://statutes.agc.gov.sg/aol/search/display/view.w3p;orderBy=date-rev;loadTime;page=0;query=ld%3Aae379db0-c3da-4abe-ada09-1d1518181ee9;rec=0#legis>, (last accessed 28 August 2017).
A. Principles

This section collects those principles articulated in other Chapters of the Report. In the final version of this Report, additional commentary regarding these Principles will also be included in this section.

Principles regarding Disclosure and Conflicts of Interest

[ALTERNATIVE A]:*

1. A party should, on its own initiative, disclose the existence of a third-party funding arrangement and the identity of the funder to the arbitrators and an arbitral institution or appointing authority (if any), either as part of its first appearance or submission, or as soon as practicable after funding is provided or an arrangement to provide funding for the arbitration is entered into.

[ALTERNATIVE B]:

1. Arbitrators and arbitral institutions have the authority to, during the selection and appointment process, expressly request that the parties disclose whether they are receiving support from a third-party funder and, if so, the identity of the funder.

[ALTERNATIVE A]:

2. For the purposes of the Principles in Chapter 4, the term “third-party funder” is defined as follows:

For the purposes of assessing potential conflicts of interest, the terms ‘third-party funder’ and ‘insurer’ refer to any natural or legal person who is not a party to the dispute but who enters into an agreement either with a disputing party, an affiliate of that party, or a law firm representing that party, in order to finance part or all of the cost of the proceedings, either individually or as part of a selected range of cases, and such financing is provided either through a donation or grant or in return for remuneration dependent on the outcome of the dispute.

[ALTERNATIVE B]:

2. For the purposes of the Principles in Chapter 4, the term “third-party funder” is defined as follows:

For the purposes of assessing potential conflicts of interest, the terms ‘third-party funder’ refers to any natural or legal person who is not a party to the dispute but who enters into an agreement either with a disputing party, an affiliate of that party, or a law firm representing that party, in order to finance part or all of the

* This Chapter presents alternative options for the Principles it articulates. These alternatives are based on continued differences that existed among Members of the Task Force and on which input during the public comment period is specifically sought.
cost of the proceedings, either individually or as part of a selected range of cases, and such financing is provided either through a donation or grant or in return for remuneration dependent on the outcome of the dispute. This definition does not extend to agreements that provide insurance or to persons who provide insurance.

Principles regarding Privilege

5. Generally, the existence of funding and the identity of a third-party funder is not privileged information.

6. Generally, the specific provisions of a funding agreement may include privileged information, and production of it should only be ordered in exceptional circumstances.

7. For information that is determined to be privileged under applicable laws or rules, tribunals should not treat that privilege as waived solely because it was provided by parties or their counsel to a third-party funder for the purpose of obtaining funding or supporting the funding relationship.

8. If the funding agreement or information provided to a third-party funder is deemed to be disclosable, the tribunal should generally permit appropriate redaction and limit the purposes for which such information may be used.

Principles regarding Costs and Security for Costs

Final award (allocation) of costs:

9. Generally, at the end of an arbitration recovery for costs should not be denied on the basis that a party seeking costs is funded by a third-party funder.

10. When recovery for costs is limited to costs have been “incurred” or “directly incurred,” the obligation of a party to reimburse the funder in the event of successful recovery is generally sufficient for a tribunal to find that a funded party comes within that limitation.

11. In the absence of exceptional circumstances, the cost of funding, including a third-party funder’s return, is ordinarily not recoverable as costs.

12. Generally, a tribunal lacks jurisdiction to issue a costs order against a third-party funder.
Security for costs:

13. Applications for security for costs should be determined irrespective of any funding arrangement and on the basis of impecuniousness.

14. In the first instance, the burden is on the moving party; no party should have to defend a motion for security unless and until the moving party makes a *prima facie* showing of impecuniousness.

15. If a party is found to be impecunious, that party should be given the opportunity to present additional evidence of funding or have a security for costs award imposed.

16. At that stage, a request for disclosure of third-party funding agreements should normally be accepted as the moving party and the tribunal should be able to examine the relevant parts of the third-party funding agreement (in particular provisions on the funder’s termination of funding rights and funder’s obligation to cover adverse costs) in the context of the security for costs application against an impecunious party. However, tribunals should limit disclosure orders to the provisions that are strictly necessary to assess the extent to which the funder may cover (or not) an adverse costs order.

17. If a tribunal decides that a security for costs order is warranted, it can order security for costs by way of a bank guarantee. Payment into a bank account may be ordered for security for costs in exceptional circumstances, and where there is no ATE or any other form of evidence of indemnification arrangements already in place.

18. In addition, an arbitral tribunal should consider indicating to the requesting party that, should the defence fail, it will be held liable for the costs reasonably incurred by the funded party in posting security. It should be for the funded party to substantiate the amount of costs it reasonably incurred in posting security.

B. Best Practices

As a starting point, there are considerable difficulties in articulating best practices that would be relevant and applicable across a range of jurisdictions, forms of funding transactions, and lawyering norms. Moreover, parties’ freedom of contract and the need for flexibility in structuring arbitral proceedings counselled against any rigid formulation. This Section provides a series of considerations that comprise best practices with respect to the funding agreement and the funding relationship.\(^{358}\)

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\(^{358}\) When the Report is finalized, this analysis of Best Practices will be supplemented to provide discussion of those Principles articulated in Chapters Four (Disclosure and Conflicts of Interest), Five (Privilege), and Six (Costs and Security for Costs).
These best practices focus on addressing those issues that arise most typically in third-party funding of claims in individual cases, and may not directly apply to other forms of funding.

1. Basic Funding Agreement Terms

(a) Funding agreements should be in writing, and their terms should be clear, unequivocal, and reflect the intentions of the parties;

(b) Funding agreements should state the amount of funding to be provided, the return to the third-party funder and how the proceeds of an award are to be distributed among the parties;

(c) Funding agreements should provide a fair, transparent, and independent dispute resolution process; and

(d) Funding agreements should include a recommendation that a party obtain independent legal advice.

Parties to the Agreement. Ordinarily, a third-party funder and a party should be the sole parties to the funding agreement in order to avoid any potential attorney conflicts of interest should the party and the funder disagree on a material issue during the arbitration. In the United States, and perhaps in other jurisdictions, the inclusion of lawyers as parties could raise concerns regarding counsel’s duty of undivided loyalty to the client.

Terms of Funding. With respect to the funding itself, a party and the third-party funder must consider and address in the funding agreement the scope and extent of the funding; i.e., whether the third-party funder will fund the arbitration through the end of the proceedings (or through enforcement), will fund up to a specific amount, will fund a specific piece of or milestone in the arbitration, or will fund the arbitration in some other fashion.

A party and the third-party funder should consider the consequences of any limitation on funding, including the cost to a party of continuing to fund the arbitration in the absence of the third-party funder’s participation, as well as the cost of enforcing any award. One key aspect that a party should consider is whether the third-party funder is basing its internal calculations on the occurrence of a certain event, such as the potential for an early settlement, thereby possibly underestimating the budget required.

A party and the third-party funder should also address which of them will be responsible for fees and costs for any related or ancillary claims, including counterclaims, and who will be financially responsible for an adverse award of costs (addressed in greater detail below).

Division of Proceeds from Award. Any agreement to fund an arbitration should specify how a future recovery will be divided between the third-party funder and a party, as noted. In general, a well-crafted funding agreement should afford a party the opportunity to retain a majority of the expected recovery (above and beyond the subject of fees and costs), based on the likeliest projected outcome. But any allocation will need to be proportionate to the measure of risk and costs assumed by a party and the third-party funder, respectively.
For example, the risk incurred by the third-party funder to pursue a successful $10 million claim will be very different from the risk on a $1 billion claim; the third-party funder’s return will also likely be different. Similarly, a third-party funder that undertakes to pursue a claim from the filing of the request for arbitration through the enforcement of the award will have considerably higher costs than a third-party funder that undertakes only to pursue enforcement of an arbitral award that has already been rendered. A third-party funder’s return may be in a fixed dollar amount, a fixed percentage, a multiple of deployed or committed capital, or a structure involving a greater of a multiple or a percentage. Any such return may also include a time-based element, and may provide a greater return to the third-party funder for longer-term recoveries.

The funding agreement should reflect the intention of both a party and the third-party funder as to the priority of the distribution of proceeds: i.e., who should be first to receive what amount, followed by the next recovery, etc. For example, third-party funders typically seek priority recovery of their principal deployed in the case before all other recoveries. Thereafter, depending on the return structure, the third-party funder, counsel and the parties may share pro rata their respective percent returns. At times, the parties may choose to establish a separate escrow account specifically created for the purpose of distributing the proceeds of an arbitration award.

Termination of Agreement or Withdrawal. Provisions for termination and withdrawal are some of the most important issues to consider in any funding agreement. In considering such terms, the parties should clearly address the following:

i. When either or both parties can terminate the agreement and on what bases, including the impact on funding already provided, any future funding, and returns due to the third-party funder, if any;

ii. Whether notice of intent to terminate or withdraw must be provided and whether it must be in writing;

iii. Whether there is a point in the proceedings after which termination of the agreement is precluded;

iv. How any amendments or modification of the terms of the agreement will be handled;

v. How differences of opinion between the third-party funder and a party concerning strategy for the conduct of the case, cooperation by the party in the case or settlement are to be resolved; and

vi. What further obligation of confidentiality is owed by the third-party funder to a party should the agreement be terminated.

Dispute Resolution Provision. In entering into a funding agreement, a party and a third-party funder should include a provision in the agreement governing how any potential disputes between the third-party funder and a party will be resolved expeditiously and efficiently. At their option, they may incorporate a mediation or conciliation step before proceeding to binding adjudication, typically private arbitration.

Transparency. A number of additional topics fall under the topic of transparency. It may be useful to consider the following in the funding agreement negotiations:
i. Whether the third-party funder is audited annually by a reputable firm;

ii. Whether the third-party funder will periodically provide a statement of the invested capital during the pendency of the case, the percentage of the budget consumed, and the risk, if any, that the budget may be exhausted;

iii. A clear expression in the funding agreement that only a party can terminate the agreement with its legal counsel, but only after notice to the third-party funder;

iv. The third-party funder should provide accurate and non-misleading information, particularly regarding its financial conditions, and its intended funding commitment; and

v. Whether and in what circumstances the third-party funder will manage a party’s litigation itself or the litigation expenses of the case.

2. Day-to-Day Case Management and Strategic Decisions (Party Control)

(a) The scope of a third-party funder’s involvement or control of day-to-day management and on all key issues such as strategy and settlement is an issue generally determined by a party and the third-party funder in the funding agreement; and

(b) The funding agreement should clearly and unequivocally reflect the intentions of the parties with respect to the scope of involvement or control on all such issues and the procedures, rights, and duties that apply when an unresolved dispute over management and strategy arises.

A key issue in any funding arrangement is determining the appropriate level of third-party funder control. Put another way, what happens when the third-party funder and a party or the third-party funder and a party’s counsel fundamentally disagree over strategy or settlement (for example, whether to accept a settlement offer or whether to add additional claims)? Some third-party funders have no interest in controlling strategy or settlement, while others believe they can meaningfully add value by contributing to or even controlling certain aspects of the case.

Some commentators contend that funding arrangements pose risks to the international arbitration process through excessive control because “the funded party becomes a proxy for the funder’s interests.”359 Although perhaps put in extreme terms, critics argue that the third-party funder “may pressure the funded party to accept certain short-cut procedures to save costs[,]” including by circumscribing pre-hearing information exchange, insisting on shortened pre-hearing written submissions or accelerated hearings, etc.360

Other commentators argue along similar lines that, although the interests of the third-party funder and a party are typically aligned to maximize the award proceeds, the arbitral process may become “flawed if not substantially corrupted” if the needs of the third-party funder mask or


360 Id., at 309.
override those of a party.\textsuperscript{361} Still others have raised the related concern that disagreements between a party (and/or its counsel) and the third-party funder could potentially create untenable conflicts of interest for a party’s counsel where the third-party funder has been retained to manage the arbitration, or retains excessive control over the proceedings.\textsuperscript{362}

On the other hand, a number of commentators have noted the extensive history of parties ceding control over litigation in both tort and insurance law contexts. According to these writers, “courts and policymakers should be sceptical of arguments that use party control as a justification to block [Third-Party Funding].”\textsuperscript{363} One scholar, Sebok, observes: “in the context of insurance law, courts have permitted strangers to take total control over a party’s litigation.”\textsuperscript{364} Others have similarly noted that insurance agreements already give the insurers the right to select counsel, decide litigation strategy, consider settlement opportunities, and impose expense audits on counsel.\textsuperscript{365} Still other commentators go further, suggesting that third-party funders should affirmatively exercise extensive control over the proceeding.\textsuperscript{366}

Although insurers can “make it very expensive for the insured to regain the freedom to tell her attorney to do things to which the funder is opposed[,] . . . this is an artifact of the terms of the contract between the client and the investor[.]”\textsuperscript{367} And as Silver succinctly summarizes, “[t]hat the client may feel pressure from the funder to follow a particular course should have no bearing on the result. Clients reject lawyers’ recommendations for all sorts of reasons, including expense, and must often make unpleasant trade-offs when doing so.”\textsuperscript{368} (In such cases, a party and the third-party funder’s dispute will be governed by the funding agreement and should not implicate the attorney).\textsuperscript{369}

Beyond commentators, there is practical experience. In Australia, for example, there exists High Court authority (and over a decade of subsequent funding experience) to support the proposition that claimants should have the right to freely choose the level of control ceded to a third-party funder, provided there is no prejudice to the court or tribunal’s process.\textsuperscript{370}

\begin{itemize}
\item Marc J. GOLDSTEIN, \textit{Should the Real Parties in Interest have to Stand Up? – Thoughts About a Disclosure Regime for Third-Party Funding in International Arbitration}, 8 Transnational Dispute Management 1 (2011).
\item Id., at 833–34, 859.
\item Id., at 838.
\item Id., n. 20.
\item See SEBOK, supra n. 12, at 856.
\item See SILVER, supra n. 15, at 638.
\item Some argue that the comparison to insurers is not apt because insurance is a highly regulated industry. However, national regulation of insurance does not always extend to the insurers’ conduct of litigation. In the United States, insurers’ control defense counsel, strategy, tactics and settlement within policy limits is typically absolute. Chapter 3 of the Report discusses control because it is often references in debates about definitions. References to control do not, however, suggest that third-party funders could not nor should not be able to contract for control over certain aspects of a funded dispute.
\end{itemize}

\textsuperscript{370} The experience in Australia in the last 10 years since the High Court’s decision in \textit{Campbells Cash and Carry Pty Limited v Fostif Pty Limited NSW} [2006] HCA 41 [Austl.]; 229 CLR 386 suggests that initial concerns that third-party funders would subvert the civil justice system there if they were allowed “control” over proceedings were unfounded. The typical provisions in Australian funding agreements enabling funded parties to override instructions
Given the historical judicial acceptance of contractual arrangements in which parties transfer control in the insurance and subrogation contexts, this Sub-Committee takes the position that a third-party funder’s control should be an issue decided by the parties during the negotiations of the funding agreement. Because there is a dearth of decisional law on point in the arbitration and litigation contexts, the parties should focus on the potential risks and concerns raised by excessive control by third-party funders during contract negotiations.

Regardless of the amount of control retained by a party and/or the third-party funder, the funding agreement should clearly reflect the parties’ understanding of who has final say on management and strategy for the funded dispute, and what happens when there is an unresolved dispute over management and strategy.

III. Due Diligence Checklist

This final section of the Chapter provides a due diligence checklist of questions and issues that funders and funded parties should consider before entering into a funding agreement.

1. Concerning the third-party funder’s legal and financial/capital structures:
   a. Is it publicly listed?
   b. Is the funder regulated and/or bound to comply with official and/or publicly published guidelines, whether having the force of law or merely by way of recommendations? Is it subject to the control of any regulating authority?
   c. Is it a limited liability company and, if so, what is its:
      (i) paid-up capital;
      (ii) objects clause;
      (iii) indebtedness and leverage level (indebtedness vs. equity capital)?
   d. Is it an investment fund and, if so,
      (i) where is it established?
      (ii) is it regulated and if so, by whom?
      (iii) what is its duration?
      (iv) What is its indebtedness and leverage level (indebtedness vs. equity capital)?

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given by third-party funders to the lawyers, and instigate a highly expedited dispute resolution process, can be described as a system of efficient checks and balances, rather than outright control.
e. Did the third-party funder take any steps to ensure that there is no actual or potential conflicts of interest between any shareholder/investor and a party, arbitrator(s), and/or opposing parties?

f. How and when does the third-party funder raise the funds necessary to fund the case? Are these funds kept in segregated accounts? If funds are subject to successive capital calls, have precautions been taken to ensure that the committed equity capital is available for the successive calls?

g. Is the third-party funder regularly reviewed by an external auditing company?

h. Does the third-party funder raise funds on a case by case basis (“pledge fund”: investors decide which case they are funding)?

2. Concerning the third-party funder’s specific obligations to a party:

a. Is the funding agreement intended to provide for the funding of the arbitration proceedings up to the stage of the rendering of an award (lawyers’ and expert(s)’ fees, arbitrators’ and arbitral institution’s fees), up to the collection of the proceeds, or up to a different milestone?

b. Is there a selective budget? Which types of costs are not included? Which precise costs/expenses are funded by the third-party funder?

c. Which aspect of the arbitration or of the enforcement is possibly not included?

d. Does the funding agreement provide for funding in respect of a potential annulment proceeding (by the respondent, by the claimant)?

e. Does the third-party funder intend to bear the costs related to enforcement of the award or related judgment resulting from the funded proceedings?

f. Does the funding agreement cover fees or costs related to ancillary claims, including defense against counterclaims?

g. Does the funding agreement address the issue of security for costs?

h. If the decisions of the third-party funder are taken by an investment (or similar) committee, does a professional arbitrator or a legal counsel specialized in arbitration participate in the decisions of the investment committee?

i. If so, how is the risk of an actual or potential conflict of interest between such person, a party, the opposing party and/or any of the arbitrators dealt with?

3. The third-party funder’s professional responsibilities

a. Does the third-party funder have an internal code of conduct or does it adhere to an external (e.g., industry) one?

b. Is the third-party funder’s code of conduct compatible with the party’s own ethical principles, and those of the lawyers representing the party?

4. The Funding Agreement

a. Who are the parties to the funding agreement?
b. Has a separate non-disclosure agreement been signed or does the funding agreement deal with confidentiality-related issues?

c. If the funding agreement sets out a pre-established budget for the proceedings, does it also provide a solution in case this budget is exceeded?

d. Does the funding agreement specify the conditions for and degree of control the funder may exercise over case strategy?

e. Does the funding agreement deal with situations of disagreement between the parties with respect to the strategy to be implemented or pursued? In particular, does it address the issue of resolution of disagreements between the third-party funder and a party concerning settlement proposals?

f. What remuneration will the funder be entitled to, and how will it be calculated?

g. Does the funding agreement include provisions regarding a potential adverse costs award against the funded party?

h. Does the funding agreement include provisions regarding who will bear the costs for enforcing the award?

i. Does the funding agreement provide for whether and under what conditions it can be terminated?

j. Does the funding agreement include provisions for modification?

k. Does the funding agreement provide for a dispute resolution mechanism in case disagreements cannot be solved amicably?
Chapter 8
Third-Party Funding in Investment Arbitration

I. Introduction

Debates over third-party funding in investment arbitration trace back to underlying differences regarding the purpose and efficacy and legitimacy of investment arbitration itself. The debate over third-party funding in investment arbitration is, therefore, infused with the underlying political dynamics of investment arbitration more generally.

Third-party funding in investment arbitration is a particularly divisive issue in a larger debate over the legitimacy of the investment arbitration regime. The range of sub-issues addressed in the earlier Chapters of this Report exist against the backdrop of these larger policy and systemic issues, but they are not necessarily capable of full consideration or resolution by arbitral tribunals in individual cases.

These complex policy issues and the competing viewpoints regarding them exist within a larger political context. Moreover, key elements of these debates are often premised on factual assumptions, for which empirical information regarding third-party funding specifically is not generally available. This Chapter does not seek to resolve the existing policy issues, but instead to outline the existing debates regarding third-party funding in investment arbitration, provide a meaningful conceptual framework for continued discussion, and propose future areas of inquiry and research as discussion and debate about third-party funding in investment arbitration continues.

Interestingly, most of the cases cited in previous chapters involving decisions over third-party funding are investment disputes and are publicly available. Instead of resolving some of the policy debates, these decisions instead appear to some to have intensified the debate over third-party funding in investment arbitration. For these reasons, the process of drafting this Report has presented many challenges, as acknowledgment of either side of the debate prompts reciprocal concerns by the other side.

Despite these formidable challenges, this Chapter aims to articulate, without fully assessing or resolving, the competing viewpoints that inform this debate. While undertaken with full acknowledgment that some views presented in this Chapter will be unpalatable to one side or the other, it is hoped that this presentation of issues will facilitate meaningful discussion during the public comment period, and perhaps beyond.

Toward that aim, this Chapter will first explore some of the policy and systemic issues that inform specific debates about third-party funding [1.]. The Chapter then proceeds to substantive issues [2.]; in particular, jurisdictional questions regarding the effect of third-party funding on investor and nationality status [A]; whether awarding security for costs protects respondent States or unjustifiably penalizes funded parties [B]; and potential conflicts of interest [C]. It will then
draw some conclusions regarding policy decisions taken by States in their domestic frameworks, in their investment treaties and by international arbitration institutions and professional organizations [D] and then identify areas for further stocktaking, research and discussions [E].

II. Policy and Systemic Issues

Many of the technical issues, including debates over disclosure and costs and security for costs, are predicated on larger policy debates about the legitimacy of investment arbitration more generally, and the role of third-party funding in that debate. In this regard, meaningful analysis can be difficult because both sides begin with underlying assumptions about the effects of third-party funding on structural aspects of the investment arbitration regime and on the rights of investors within that regime.

On one side of the debate, investment arbitration may be regarded as a legitimate process only to the extent it facilitates and promotes investment seen as an engine for sustainable economic and social development. Under this view, certain categories of cases are considered directly objectionable, and the overall rise in the number of cases—sometimes attributed to third-party funding—has also been an independent cause for concern. The profit incentive of third-party funders is often regarded as inherently incompatible given that arbitral awards are paid from public funds. The notion that some amounts recovered from States would go to third-party funders, instead of solely to aggrieved investors, is considered inconsistent with the underlying goal of promoting sustainable development.371

On the other side of the debate, investment arbitration is regarded as an essential means of providing recourse for foreign investors when governments act in ways that violate applicable treaty-based protections for their investments such as protection against expropriation, discrimination or violation of an obligation to provide fair and equitable treatment or full protection and security. Under this view, third-party funding is an essential tool for facilitating access to justice, particularly for that class of investors whose investments have been wrongfully expropriated and therefore would lack the means to pursue an investment claim in the absence of third-party funding.

Even for those claimants whose investments have not been expropriated, the argument goes, investor-claimants should not have to forego business opportunities by using their own capital to pursue recourse for harms allegedly caused by the wrongful conduct of a State.

Alternative means of financing claims allows claimants to minimize continued harm from the alleged misconduct, and strategically reduce the risks of pursuing the claims. It is also argued, more generally, that modern third-party funding is not functionally or economically different from alternative means of financing claims, such as contingency fees and certain types of insurance. Under this view, modern third-party funding should not be singled out for different treatment particularly with respect to security for costs.

While these opposing views continue to animate discussion on specific topics relating to third-party funding, as a practical matter they do not move the needle very much. Recent legislative trends are increasingly permitting third-party funding, and no meaningful effort has been made to preclude third-party funding in investment arbitration. Instead, all recent reforms appear to acknowledge implicitly that third-party funding is now there to stay and must be accepted. Where the efforts of regulating and framing third-party funding have gone and could be going in future is towards more transparency. Questions remain about the extent and limits of such transparency, particularly in light of the potential for time-consuming and expensive procedural abuses and the implication of confidential information.

With third-party funding now regularly involved in investment arbitration, there are also more specific policy debates about its effect on caseloads, costs, and investor rights. One of the most common arguments from critics of third-party funding in investment arbitration is that it supports or encourages the bringing of claims that would otherwise not be brought. This critique falls into two categories.

The first area of concern is that third-party funding increases the overall number of investment arbitration claims brought against States. This argument ties into related concerns that, as damages are the primary remedy in investment cases, the effect of alleged expansion would disrupt the balance between investor protection and State interests.372

The second, more particular objection is that third-party funding increases not simply the number of cases generally, but the number of speculative, marginal, or frivolous investor claims. Proponents of this view point to the high recoveries sought by claimants,373 which they argue creates an incentive to fund even cases with a low probability of success because any single success can cover the cost of funding a portfolio that includes other cases that are likely to fail. Notably, there is no clear empirical evidence about whether the increase in investor claims is indeed related to third-party funding, or more specifically about whether funding is increasing the number of

373 Liang-Ying TAN and Amal BOUCHENAKI, Limiting Investor Access to Investment Arbitration: A Solution without a Problem? in Jean E. KALICKI and Anna JOUBIN-BRET, Reshaping the Investor-State Dispute System, (Brill 2015) p. 250 (identifying perceptions that some investment arbitration decisions “award unrealistic and unfair damages to claimants with insufficient regard to public interest, national security or other extenuating circumstances.”).
speculative, marginal, or frivolous cases, given the lack of information or empirical research about the participation of third-party funding in individual cases.

Several responses are offered to these critiques. First, funders argue that such concerns are premised on a misunderstanding of the processes by which funders select cases. As described in Chapter 2, before deciding to fund a case, a funder engages in a rigorous assessment of the claimant’s likelihood of success on the merits. The result of this rigorous review, funders report, is that they decide to fund only those cases that are deemed to be highly likely to succeed, which translates into a tiny fraction of cases in which funding is sought. Anecdotally, the funders on the Task Force and those queried in preparing this Report suggest they fund only about one in ten cases for which funding is sought.374

Of the cases that qualify for and receive funding, funders report that many of those cases could not be brought in the absence of funding. As a result, they argue, third-party funding operates to provide access to justice that would otherwise be denied to genuinely aggrieved claimants. Relatedly, funders report that some claims for which they forecast a high likelihood of success on the merits do not provide the potential for sufficient return on investment. As a result, some investors are still unable to bring legitimate and potentially meritorious claims. Under this view, even if third-party funding raises the overall number of cases brought, that increase is among presumptively meritorious claims and is attributable to other causes (the increased number of BITs, unlawful behaviour by States, etc.), which account for the increase in cases.

One problem in attempting to sort through these competing arguments is that they arise in the context of larger debates about the legitimacy of investment arbitration. Accordingly, even if most may agree that access to justice is an important goal, they cannot agree on what constitutes a frivolous, marginal or speculative case since that determination is effectively only made once the claims have been rejected by a tribunal, after considerable expense has been incurred by the two sides in dispute.

Critics note that at least some claimants with third-party funding have brought claims that tribunals determined were frivolous or otherwise associated questionable conduct by claimants with funders.375 Building on this background, some argue that the risks are particularly acute in investment arbitration because of the conditions for jurisdiction and admissibility are stringent and standards of protection in investment treaties, especially fair and equitable treatment, remain vague. As these standards have been broadly developed, they argue, the system is endangered not only by frivolous claims, but also by claims that are speculative or seek to expand the bases for liability for States beyond the originally intended meanings in investment and trade agreements.

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374 See Chapter 2, at p. 56.
The primary response to these concerns is that third-party funders do not intentionally fund frivolous cases because it goes against their business model. Moreover, the risk of unintentionally funding a potentially frivolous case is low because of the extensive due diligence funders engage in as part of their decision about whether to fund a case. In support of these views, funders report that they generally fund only one out of every ten cases in which funding is sought. These views have been articulated publicly by many funders and attorneys who have worked with funders, and were underscored in Task Force discussions.

Despite instance that the funding of frivolous, or even high risk, cases could never be good for business or part of an overall strategy for funders, critics of investment arbitration seem as yet unconvinced. One reason might simply be lack of understanding about how funding works. In this sense, it is hoped that the work of the Task Force and the explanations in Chapter 2 of this Report will promote clearer understanding of criteria and processes for selecting cases.

Another possible basis for continued scepticism is that not all funders are created equal. In fact, since constitution of the Task Force, the number of funders has increased significantly, with new venture capitalists and in some instances banks announcing they are “entering this space” (meaning financing of investment arbitration claims). In fact, some cases cited in this Report would seem to illustrate critics’ worst fears about funders. In a field as politicized as investment arbitration, it is perhaps not surprising that these cases may have taken on exaggerated importance. To critics, they are taken as exemplars of all their worst fears about third-party funders, even if many would describe them as anomalous outliers that are not representative.

This debate about the overall impact of third-party funding is not unique to investment arbitration. Similar arguments have been raised with respect to litigation funding in national courts. For example, in the United States, in a petition written by the U.S. Chamber of Commerce and signed by the International Association of Defense Counsel, one argument advanced was that funding would result in an "expected … increase the filing of ill-considered cases." There has been some limited empirical research regarding litigation in national courts. For example, a recent study examined the effects of third-party funding in litigation in Australian courts, and concludes that third-party funding leads to an overall increase in the number of claims being brought. It also concluded that third-party funders have funded cases that raise novel issues and involve riskier, more uncertain claims, and that decisions in funded cases were particularly influential in developing the law as they were reversed less and cited more than non-funded cases. By contrast,
another study of funding of personal injury claims in The Netherlands suggests that greater availability of funding does not lead to an increase in the overall number of claims filed.380

Studies of trends in domestic litigation do not necessarily translate into investment arbitration. Meanwhile, there are numerous practical obstacles to doing similar empirical research in the investment arbitration context. To the extent such research is undertaken, three important features of investment arbitration will need to be considered: 1) the high values for relief sought; the high cost of pursuing claims in investment arbitration; and 3) the fact that States can only be responding parties.

Critics argue that if claimants and funders are not compelled to pay the respondent State’s costs when they lose, they have an incentive to bring risky claims.381 Meanwhile, the high cost of pursuing claims make access to justice issues particular poignant, and the need for funding increasingly relevant. However, here again, critics argue that third-party funding contributes to inflating the damages sought and the costs of pursuing such claims.

Notably, most recent investment and trade agreements, while attempting some procedural changes, do not preclude or even limit the use of third-party funding.382 Instead, the focus is on transparency and on disclosure of the existence and, in some instances the terms of a funding arrangement by a third-party funder. Although few examples are available publicly apart from Comprehensive Economic and Trade Agreement (CETA) between Canada and the European Union,383 some proposed language from draft model investment treaties were presented during Task Force discussions

III. TECHNICAL AND DOCTRINAL ISSUES

A. JURISDICTIONAL QUESTIONS ABOUT THE EFFECT OF THIRD-PARTY FUNDING ON INVESTOR & NATIONALITY STATUS

Third-party funding raises some specific issues in investment arbitration given the language of investment treaties or investment contracts where the subject matter of investment and

380 Michael G. FAURE, Ton HARTLIEF and Niels J. PHILIPSEN, “Funding of Personal Injury Litigation and Claims Culture: Evidence from the Netherlands”, 2 Utrecht L. Rev. 1 (2006) (finding that Between 1999 and 2003, the number of policies for legal expenses insurance increased by over 30 percent, but the number of personal injury claims remained stable).
381 RSM Production Corporation v. Saint Lucia, (ICSID Case No. ARB/12/10), Assenting Reasons of Gavan Griffith (12 August 2014).
382 CETA Article 8.
the investor are precisely defined and often give raise to jurisdictional and admissibility objections. Potential jurisdictional issues relating to the status of the investor. Jurisdiction in investment arbitration is premised on requirements that the claimant “be a covered ‘investor’, carry the nationality of one of the contracting parties, and hold a protected ‘investment’ in the territory of the host state.” Out of these requirements, with respect to third-party funders, two questions have been raised:

1) whether the participation of a funder may change the status of, and therefore disqualify, a claimant from qualifying as an ‘investor’; and

2) whether third-party funding itself may qualify as an ‘investment’.

These questions can be complicated to answer since the modern forms of non-recourse financing in exchange for a percentage of any potential recovery is now but one of many possible forms. Third-party funding increasingly involves complex and diverse funding structures, which has prompted arguments in some cases that the participation of a third-party funder or transfer or transfer of economic interests may affect the claimant’s status as an investor and its nationality.

Before turning to these arguments, it is worth noting that modern third-party funding has been a specific focus for this argument, but the same and similar arguments could be raised with respect to other funding mechanisms that are functionally similar to modern third-party funding. For example, political risk insurance (PRI) is an important means of encouraging investment, and typically requires the claimant to subrogate the claim to the insurer. As Mark Kantor explains:

[B]y operation of the doctrine of subrogation and the express terms of the PRI programs operated by public insurers like OPIC and MIGA, the insurance provider automatically steps into the shoes of the investor and succeeds to the investor’s claim against the State upon payment under the PRI policy. The subrogated PRI provider is then entitled to pursue that claim against the expropriating State directly – in fact, ordinarily by means of arbitration[.]
PRI has generally been regarded as a valuable tool for increasing the flow of foreign investment to developing and emerging economies that need such investment, and claims are routinely brought by subrogated insurers through arbitration. Such claims are not usually brought directly under the investment treaty, and therefore do not directly raise the same issues. Perhaps for this reason, and perhaps because some of the most prominent forms of PRI are government or international organization – sponsored and part of the same package as bilateral investment treaties providing the protection, PRI has not generally been subject to the same criticisms as third-party funding and subrogation practices with respect to insured claims have likewise not raised jurisdictional challenges.

By contrast to the general acceptance of PRI, modern third-party funding by private entities has been met with jurisdictional challenges. For example, the Respondents in Teinver S.A. v. Argentine Republic challenged jurisdiction based on an assignment. Respondent argued that “once the assignment is made, the assignor is replaced in the proceedings by the assignee, which has not been the case in this arbitration proceeding.” Under this view, the funder, not the claimant, became “the real party interested in this arbitration” after the assignment, a point supported by the fact that only the funder “would seem to be potentially benefited in the case of a hypothetical award against Argentina in the instant case.”

Claimants’ primary response was related to timing— the funding agreement was entered into after that there was “no applicable legal standard that would prevent this Tribunal from issuing an award of damages in Claimants’ favour due to the assignment agreement.” The Tribunal did not decide the issue in the decision on jurisdiction and left it for the final award. In the final award, the Tribunal found that the assignment was not for “contentious claims” but rather for the “proceeds from any award issued” and, therefore, in the eyes of the Tribunal no assignment occurred that affected Claimants’ standing in the proceedings.

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391 Ibid p. 60.

392 Ibid p. 60.


Another line of investor-State cases took up related challenges that various forms of funding may be a de facto “transfer of case control to a funder before the initiation of arbitral proceedings” that may “lead to a change of the claimant’s identity, and thus does not affect the admissibility of a funded investor’s claim”. In some cases, tribunals relied on the timing of any alleged transfer of control to conclude that the role of a third-party funder does not affect jurisdiction.

For example, in CSOB v. Slovakia, CSOB assigned its claims to its home State. In concluding that it retained jurisdiction, the tribunal reasoned that “the transfer of rights after the institution of proceedings should not be taken into account at all, and consequently cannot affect jurisdiction.” Another tribunal, with reference to CSOB v. Slovakia and related case law from the International Court of Justice, found that “once established, jurisdiction cannot be defeated […] it is simply not affected by subsequent events […] this principle applies in particular to the nationality requirements under Art. 25 of the ICSID Convention.”

The decision in RosInvestCo UK Ltd. v. The Russian Federation, went further, concluding that timing was not the primary consideration. The tribunal in that case concluded that even a funding agreement entered into before the initiation of arbitral proceedings would not affect the meaning of the terms “investment” and “investor.” The tribunal in RosInvestCo reasoned that the assignment from RosInvest “to a funder of a different nationality than the funded party before the initiation of the arbitral proceedings does not affect jurisdiction” unless the relevant investment treaty states otherwise in clear language. As a consequence, the tribunal concluded that financing for a claim does not affect jurisdiction for the arbitration.

Based on these arbitral awards and in the absence of any new investment treaty language, the existing position in investment arbitration appears to be that third-party funding, regardless of the form, does not alter the national identity of a claimant and hence the jurisdiction of arbitral tribunals. This outcome arguably produces a result similar to the long-established use of political risk insurance, and the practice of subrogating claims that is typical in that context because, as analyzed in Chapters Two and Three, subrogation can fit within some definitions of third-party funding. Although a similar outcome is reached through subrogation in the PRI context, the claims are actually brought pursuant to a separate arbitration agreement, so does not directly implicate the technical definitional issue.

396 As noted in Chapters 2 and 3, the extent and nature of control exercised can vary both among funders, and among funding agreements.
399 Ibid at p. 233 (“The award in RosInvest provides considerable support for the position that a litigation funding agreement does not negatively affect jurisdiction, even if concluded before the date the proceedings are initiated.”).
400 Ibid at p. 239.
This position is also consistent with the use of contingency and conditional fees, which in many respects are functionally equivalent to third-party funding, but likewise have not been asserted as a basis for challenging jurisdiction. Moreover, given that the few known treaty revisions that address third-party funding have focused on disclosure issues, it seems unlikely that States are or will seek to introduce provisions that affect investor or nationality status based on funding.

[B] SECURITY FOR COSTS: NECESSARY TO PROTECT RESPONDENT STATES VS. UNJUSTIFIABLY PENALIZING FUNDED PARTIES

The legal frameworks and practical considerations regarding costs and security for costs, in both investment and international commercial arbitration, are analyzed in Chapter 6. The conclusions there, based on analysis of existing sources and reported investment arbitration cases is that the existence of third-party funding is generally irrelevant to either a determination of a request for security for costs or a final allocation of costs at the end of the case.\(^{401}\) The Task Force concluded that the principles articulated are a sound reflection of existing standards and economic principles that affect analysis in particular cases. It nevertheless recognized that these issues can also implicate larger macro-economic and structural debates in investment arbitration, which are reflected on briefly in this Section.

State parties and critics often tie their concerns about third-party funding to structural issues regarding increasing investment arbitration caseloads and the potential financial strain on States.\(^{402}\) This concern stems from the fact that in investment treaty arbitration, States are always respondents and are not able to bring counter-claims. Even when a State prevails, it does not receive compensation and will have to pay for the costs of its own defence. Funding is now available (albeit on a very different basis, typically more akin to after-the-event insurance) for responding States. One of the most prominent examples of third-party funding of a respondent State is the financial support for Uruguay in the *Philip Morris v. Uruguay* case.\(^{403}\)

In this context, security for costs and allocation of costs at the end of case are regarded as a means of deterring frivolous claims and ensuring that, if the respondent prevails and is awarded costs at the end of the case, a losing claimant will be able to pay the adverse costs award.\(^{404}\)

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\(^{401}\) For a discussion on existing standards for allocating costs and granting security for costs, see Chapter 6.


\(^{403}\) “The Anti-Tobacco Trade Litigation Fund”, available at <http://global.tobaccofreekids.org/en/about_us/trade_litigation_fund/> (last accessed 27 August 2017) (“The fund will support lower- and middle-income countries that have been sued by tobacco companies in arbitration under international trade agreements. Managed by the Campaign for Tobacco-Free Kids, the fund will provide financial and technical assistance to governments committed to defending their laws to reduce tobacco use.”).

\(^{404}\) See Memorandum of 12 June 2016 from Iván A. ZARAK, Acting Minister of Economy and Finance of Panama, to Meg Kinnear, International Centre for Settlement of Investment Disputes, available at...
increasing number of investment arbitration cases raises concerns about States’ ability to offset the costs of responding to such cases, particularly small States and States facing domestic economic challenges. These concerns were historically also accompanied by assumptions that the provision of third-party funding necessarily implied a funded party was impecunious or would otherwise be unable to satisfy a potential costs award.

Today, as described in Chapter 2, the assumption that funding necessarily signals an impecunious claimant is no longer sustainable. As noted above, it can provide resources for a respondent State, and is increasingly being undertaken not out of financial necessity, but as a means of allocating corporate resources and risks. Nevertheless, there are still many cases in which claimants seek funding because they do not otherwise have the resources to pursue those claims. In this category of cases, however, third-party funding can enable a party that has had all of its assets wrongfully expropriated to nevertheless pursue a remedy. In such a case, an order for security for costs would penalize a party for not having resources, even though its lack of resources was caused by the responding State’s allegedly improper expropriation of its assets.

On this issue, the prevailing view among respondent States and related stakeholders is that it would be particularly unfair, now that the trend is for costs to follow the event, if a prevailing State cannot collect costs against an impecunious claimant or be reimbursed by the third-party funder that was prepared at the outset to share in the risk of making a potential gain. As noted by Panama in its recent letter to ICSID, an increasing number of enforcement cases are being brought by prevailing States before the domestic courts in an investor’s home State.

On the other side of the spectrum, some argue that the monitoring of fees and expenses by third-party funders may generally reduce the overall cost of obtaining a successful award. Given their incentive to keep legal costs within predicted budget projections, the argument is that they may be more focused on efficiency than law firm representation based on a straight hourly rate.

Another recurring argument raised by funders, however, is that when the presence and identity of a funder is revealed, respondents use the disclosure as a basis for bringing challenges to arbitrators, requests for further disclosure, and requests for security for costs. These reactions to disclosure of funding arrangements can slow arbitral proceedings considerably, and consequently significantly increase the costs of an arbitration. Funders and funded parties argue that many of these efforts are substantively unfounded and are instead tactics to delay proceedings and increase the costs of proceedings to make the funding model untenable. In fact,


405 See Chapter 2, at p.13 (describing why parties seek funding, and different types of financing or insurance that can provide for satisfaction of an adverse costs award).

406 Funders’ cost-monitoring function has raised some questions about attorneys’ independent professional judgments. These issues are generally the province of national ethical rules and the funding agreement, and for these reasons not considered directly in this Report, other than generally in Chapter 7 in a discussion of Best Practices. See Chapter 2, at p. 20; Chapter 7.

407 Unforeseen delays or increases in legal costs can change the assumptions on which funding was provided and make otherwise potentially meritorious claims unprofitable from the funder’s perspective. See Chapter 2, at p. 20.

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the potential for such challenges is the primary reason why funders express reluctance at having their presence and identity disclosed.

Debates about costs and security for costs, and the existing standards articulated in Chapter 6, are being challenged based on larger macro arguments about structural incentives and disincentives, and the ability of States to effectively recover costs that they may be awarded at the end of a case, described above in Part I of this Chapter.

Some funders have argued that security for costs does not have a place in arbitration generally. Under this view, the risk of an unenforceable award (including an unenforceable award for costs) is like any litigation risk, and should not be treated differently in the investment context. Systematic issuance of security for costs orders will simply raise the cost of third-party funding for investors, which will translate into reduced recovery margins for funders or a restriction on the availability of funds. Either scenario, it is argued, will reduce the ability of genuinely aggrieved investors to access justice.

Other funders have argued that they are rather agnostic about the imposition of security for costs because any costs added by such an order can simply be added into the funding agreement. The greater problem, under this view, is uncertainty about whether security for costs will be granted. In a related vein, at least one tribunal has found that the existence of after-the-event, or ATE, insurance is sufficient security and no order is necessary. As described in Chapter Two, this type of insurance can be purchased to provide for coverage in the event a claimant is liable for adverse costs. Indeed, in *Eskosol S.p.A. v. Italy*, the tribunal found that Italy’s request for security for costs was not urgent because the claimant had purchased ATE insurance.408

Premiums for ATE or added financial burdens to cover a potential adverse costs in a funding agreement may still raise questions. On the one hand, particularly for claimants in financial difficulties, they may not be able to afford the premiums for ATE insurance. Alternatively, the inclusion in a funding agreement of coverage for a potential adverse cost award necessarily raises the cost of securing such funding. A reasonable argument could be made that ATE or coverage in a funding agreement can be a workable alternative to an order for security for costs, and can provide a benefit to all by avoiding the added delay and expense that comes with an application for such an order. A natural question, however, might become who pays for the cost of such security in the event a responding State loses, and how might the cost savings of translating this point of contention and uncertainty into a more simple question of insurance and structural planning.

C. Potential Conflicts of Interest

408 See *Eskosol S.p.A. v. Italy*, ICSID Case No ARB/15/50.
409 See Chapter 6, at p. 134.
The issue that has attracted the most attention regarding third-party funding is with respect to arbitrator’s potential conflicts of interest. As with parties and law firms, an arbitrator may have potential conflicts of interest with third-party funders. Until recently, however, the existence of funding and identity of funders was not disclosed to facilitate assessment of potential conflicts by arbitrators.

As part of their rigorous assessment of a case prior to agreeing to funding, particularly in the context of investment arbitration where a number of technical and substantive issues as well as high amounts at stake make the funding more risky, funders recurrently ask for first or second opinions from experienced arbitration lawyers, often arbitrators themselves. Some examples of reputed arbitrators sitting on the board of funds or acting as advisors have made headlines of professional press.\(^{410}\) Meanwhile, as noted, disclosure has led to what some contend are unfounded challenges to arbitrators.

Chapter Three of this Report examines recent developments, introduced by various arbitral institutions, national regulators, international trade agreements, and international soft law, which increasingly require disclosure about the identity of funders to enable arbitrators to assess potential conflicts of interest. Chapter Three proposes that the existence and identity of a funder be disclosed, either as a matter of course or in response to a request from an arbitral tribunal or institution. It does not, however, propose any new standards for substantively assessing potential conflicts of interest, but instead leaves such assessment to existing standards. This trend has been followed also in the context of investment arbitration either by States in their recent treaties or by arbitral institutions. As indicated earlier, the fact that third-party funding is now part of the picture is acknowledged but regulated and framed by provisions requiring disclosure. The trend is particularly strong in investment arbitration given the underlying goal of achieving more transparency to alleviate concerns about the system itself and increase its legitimacy.

**D. Recent moves towards regulating third-party funding in investment arbitration**

Notably, neither the IBA Guidelines nor the Principles in Chapter Three of this Report are formally binding, and the ICC Guidance Note is also similarly an advisory,\(^{411}\) not mandatory

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instrument. Meanwhile, the SIAC Investment Arbitration Rules 2017 expressly authorize arbitral tribunals to require disclosure of third-party funding, but they do not require such disclosure.412 The only mandatory disclosure requirements that apply to international arbitration appear to be the national legislative reforms in Hong Kong and Singapore, and a few provisions in investment treaties.413

ICSID has recently announced that it will be considering rules governing disclosure of third-party funding as part of its process of updating its rules and regulations.414 It remains to be seen whether ICSID and other institutions will mandate systematic disclosure of funding and the identity of funders or, consistent with the approach of the SIAC Investment Arbitration Rules, simply authorize arbitrators to order such information.

IV CONCLUSION

As noted in the introduction, this Chapter does not seek to provide concrete answers to the larger considerations and policy debates in which third-party funding issues are often raised. Instead it aims to provide a fair-minded presentation of competing viewpoints in the larger political debates, sharpen the focus of such debates and, in this conclusion, suggest some possible areas for future research and work.

As described in Chapter One,415 the central purposes of the Task Force include promoting a clearer understanding of issues relating to third-party funding and engaging a range of stakeholders in meaningful dialogue about those issues. From this view, the Task Force’s means were an end in themselves. In the work of the Task Force itself, Members shared generously from their experiences and distinct perspectives, but also listened and engaged in dialogue that, at least in some instances, changed otherwise settled minds. It is hoped that, through this Draft Report, the public comment period, and publication of the final Report, the work of the Task Force will provide for better composite understandings of the issues and greater appreciation of the reasons for differing viewpoints.

413 See Chapter 3.
415 See Chapter 1, at p. 2.
Dialogue alone will not, of course, necessarily produce consensus. In fact, even after extensive discussions, many areas of disagreement remained among Task Force Members. Particularly as the number of third-party funders and funded cases increase, and the pace of related reforms quickens, and as public scrutiny remains trained on investment arbitration, the need for constructive dialogue has never been greater.

Meaningful and engaged dialogue can help identify more clearly areas of actual agreement and disagreement, sharpen focus and analysis, and help collectively distinguish between what are priorities and what is background noise. At a minimum, some collective understandings can help identify the critical issues for sustained independent empirical research that is needed to bring clear-eyed assessment to some of the factual assumptions that animate arguments on both sides. It is also at least possible that such dialogue may also facilitate some creative solutions to seemingly entrenched opposition on issues relating to third-party funding. In this respect, the Task Force hopes that input received during the public comment period will further advance our understanding.
Agenda

1. Background
   a) Financing commercial litigation
   b) Defining litigation finance
   c) How clients and law firms use litigation finance

2. Ethical considerations
   a) Champerty, maintenance, barratry
   b) Usury
   c) Work product
   d) Attorney-client privilege
   e) Common interest exception
   f) Confidentiality
   g) Potential conflicts of interest
   h) Control of counsel, strategy and settlement
   i) Independent judgment
   j) Zealous advocacy

3. Practical application
   a) Role of the funder
   b) Process, criteria
   c) Assessing potential funders
   d) Code of conduct
Background
Definitions, types and uses
Financing commercial litigation

The financing of commercial litigation takes many forms

- Commercial plaintiffs may self-finance claims by drawing on existing credit sources, accessing venture capital, and seeking capital from investment banks, funds and private investors.

- There is an active market in commercial claims; owners of claims can easily sell or assign them to economic actors interested in pursuing them.

- The assets underlying claims (or related debt or derivative instruments) are frequently bought and sold to extract the value associated with the claim through litigation, in both insolvency and non-insolvency contexts.

- Contingency fees for commercial claims are widely available, from both traditional contingency plaintiffs’ firms and from many hourly firms.

- Insurance and reinsurance are widely used in all stages of litigation process.

- Over the past decade or so, specialist providers of litigation finance have joined this field, growing significantly as the demand for outside capital to finance commercial litigation has outstripped the supply from traditional sources.
Defining litigation finance (1/2)

Burford is the leader of this fast-growing field

• Value of litigation claims is used to obtain financing
• Capital is provided on a non-recourse basis, in exchange for return tied to case outcome
• Financial burden is lessened for litigants with fee fatigue or in need of alternative fee structures
• Used by firms to expand contingency fee or alternative fee practice, manage risk and cash flow
• Payment of litigation-related receivables can be accelerated

40% of clients have actively asked about litigation finance

Source: 2016 Litigation Finance Survey
Defining litigation finance (2/2)

Burford is the leader of this fast-growing field

- Evolving into “corporate finance for law”
- Capital used to cover fees and expenses as well as other business and firm needs
- Applicable to both claimants and defendants
- Embraced by clients from small businesses to the Fortune and FTSE 500
- Relevant to all firms regardless of business model (contingent or hourly)
- Increasingly moving from single case funding to portfolio arrangements
- Provide capital to firm across pool cases
- Because risk is diversified, particularly relevant for high-risk matters (patent, arbitration, bankruptcy)
“Hundreds of companies, increasingly from the Fortune 500, have used litigation finance, convinced it was in their interest.”

– The New Yorker
How clients use litigation finance

**Innovative vehicles on the rise**

- Finance a single case or portfolio of cases, shifting cost and risk of bringing major commercial litigation or arbitration
  - Non-recourse funding of legal fees and expenses
  - Working capital for operations
- Hybrid structures using a combination of recourse and non-recourse financing
- Share risk of fee-shifting in certain cases
- Accounting advantages
  - Improves operating cash flow by removing litigation cost from above-the-line expenses

**Composition of new litigation investment commitments made in 2016**

- Single 12%
- Portfolio & complex 88%

Source: Burford Capital Annual Report (2016)
How firms use litigation finance

• Non-recourse capital to the firm
• Functions as “hybrid contingency” for hourly clients under pressure to reduce fees
• Enables hourly firms to pitch expanded service without increasing cost
• Capital for individual large-dollar contingency or alternative fee matters
  – Reduce contingency risk for ongoing pre-trial litigation
  – Monetize expected fee after trial, pending appeal
Basic model for litigation funding*

Litigant and funder

- **Law Firm**
  - Payment of litigation fees and expenses on behalf of client
  - Engagement agreement (discounted hourly or hybrid)
  - Capital provision agreement
  - No change in relationship between client and firm

- **Client**
  - Client Proceeds Net of Burford Return

- **Burford**
  - Burford Return

- **Settlement or Award Proceeds**
  - Flow of litigation proceeds based on successful outcome

- **Lawyer Success Fee (if any)**

*Conceptual structure; does not reflect terms*
Basic model for portfolio finance*

**Law firm and funder**

- **Clients**
  - Contingency engagement agreements
  - Payment of contingent litigation fees and expenses

- **Law Firm**
  - Capital provision agreement
  - Payment of contingent litigation fees and expenses
  - Payment of Burford’s return per funding agreement
  - No change in relationship between client and firm

- **Burford**

- **.client Proceeds**
  - Settlement or Award Proceeds
  - Law Firm Contingency Fee

- **Litigation Opponents**

*Conceptual structure; does not reflect terms*
Ethical considerations
Relevant ethical topics and rulings
Ethical considerations

Overview

• Chief areas of ethical consideration pertain to
  – Engaging an outside funder that will have a financial stake in the outcome of litigation
  – Sharing information that a litigation finance provider will require in order to invest in a matter without risking waiver of protected communications
  – Ensuring that client’s interests are paramount regardless of a relationship with an outside funder

• Presence of funder does not change attorney/client relationship
  – Litigation finance provider has no control over litigation strategy or settlement decisions

• Funder may consider privileged information
  – Parties execute NDA before any substantive discussions
  – Good case law in key jurisdictions confirming work product protection applies to funder communications and documents
  – A good litigation funder will be vigilant in managing relationship to avoid risking waiver of protected communications
“The tired debate about litigation finance in the U.S – whether it is a path toward runaway frivolous litigation or provides increased access to justice – is essentially over, with the latter view prevailing. With very view exceptions, most states have accepted the validity of third-party funding in the context of large, complex litigation.”

– Bloomberg Law, January 11, 2016
Champerty, maintenance, barratry & usury

• Maintenance
  – Helping another prosecute a suit. “[T]he officious intermeddling in a suit, ‘for the purpose of stirring up litigation and strife, encouraging others to bring actions or make defenses that they have no right to make’”

• Champerty
  – Maintaining a suit in return for a financial interest in the outcome

• Barratry
  – The continuing practice of maintenance or champerty is sometimes referred to as barratry

• Usury
  – Charging interest at a rate that exceeds a maximum rate provided by law for the particular category of lender involved
Champerty (1/5)

• Concept first developed in modern law by the Church and became part of English law during the time of the medieval feudal system

• Intended to prevent powerful landowners from helping their tenants mount lawsuits to “oppress” others by subjecting them to litigation. Thalhimer v. Brinckerhoff, 3 Cow. 623 (N.Y. 1824)

• By the 1900s, England had concluded that maintenance and champerty were “dead letters that were no more than useless ‘lumber’”. (Lord Neuberger, From Barretry, Maintenance and Champerty to Litigation Funding, Speech at Gray’s Inn, May 8, 2013, available at http://www.supremecourt.gov.uk/docs/speech-130508.pdf., at 6)
Champerty (2/5)

*Approaches to common-law champerty vary among states*

- Never adopted from England or was adopted and later abandoned: Arizona, California, Colorado, Connecticut, Idaho, New Jersey, New Hampshire, New York, Texas, Michigan and Montana
- Overruled by legislation: Maine, Ohio, Tennessee, Virginia
- Struck down or severely limited by courts: Hawaii, Iowa, Massachusetts, South Carolina, New Mexico, Nevada, Florida, Maryland, North Dakota, Oregon, Washington, West Virginia, North Carolina
- Recognized only as a defense to enforcement of an allegedly champertous agreement: Georgia, Oklahoma, Alaska, Nebraska, Pennsylvania, South Dakota, Wisconsin
- Applied to assignment of entire claim (as distinct from litigation finance): Delaware, District of Columbia
- May have some vitality: Mississippi, Arkansas, Alabama, Illinois, Minnesota, Missouri, Kentucky, Rhode Island
Champerty (3/5)

• Rulings in the US Federal courts and opinions from various bar associations suggest that laws concerning champerty, maintenance and barratry are outmoded and have no bearing on complex commercial litigation finance
  – “The consistent trend across the country is toward limiting, not expanding, champerty’s reach.” Del Webb v. Partington (9th Cir. 2011)
  – ABA Commission on Ethics 20/20 Informational Report to the House of Delegates (at 9–10): “It is unclear why the historical concerns of the common law would justify today placing special burdens on litigation funded by third parties.”
  – Charge Injection Technologies, Inc. v. E.I DuPont de Nemours & Co., (Del. Super. Ct. Mar. 9, 2016): The provision of litigation finance constituted neither champerty nor maintenance. The court described the role of the litigation financier as that of a passive capital provider with no control over litigation or settlement
Champerty (4/5)

• Modern-day litigation has evolved since the ancient rule of champerty and its cousins were created; concepts such as Rule 11 and a strong independent judiciary have taken their place.

• Even in states with champerty laws still on the books, they are not being used to interfere with legitimate, good faith commercial litigation financing transactions; those transactions permissible as long as the supplier is not:
  – Promoting frivolous litigation
  – Intermeddling with conduct of litigation
  – Engaging in “malice champerty” (supporting litigation with improper motive)

• These are not considerations for established commercial funders
  – Funders want to win and seek meritorious cases
  – Funders are largely passive, do not control litigation
Champerty (5/5)

Statutory Approaches to Champerty

• A limited number states have adopted statutes that emulate common law champerty
  – New York Judiciary Law § 489 prohibits the purchase of any financial instrument or claim “with the intent and for the purpose of bringing an action or proceeding thereon”
    ▪ Misdemeanor, also can be raised as a defense to litigation brought pursuant to a champertous purchase
    ▪ Safe harbor where the purchase price exceeds $500,000
    ▪ Justinian Capital SPC v WestLB (N.Y. 2016) – The safe harbor can apply in a variety of structures, so long as there is a binding and bona fide obligation to pay $500,000 or more for notes or other securities, which is satisfied by actual payment of at least $500,000 or the transfer of financial value worth at least $500,000 in exchange for the notes or other securities.
    ▪ Trust for the Certificate Holders of the Merrill Lynch Mortgage Investors, Inc. v. Love Funding Corp., 13 N.Y.3d 190 (N.Y. 2009) – Section 489 does not apply when the purpose of an assignment is the collection of a legitimate, preexisting claim.
  – Official Code of Georgia § 13-8-2(a) explicitly names “contracts of maintenance or champerty” as contrary to public policy and thus unenforceable
  – In Illinois, 720 Ill. Comp. Stat. 5/32-11 and -12 prohibit intentional barratry and maintenance
    ▪ Requires the champertor to “officiously intermeddle” in an action; so long as a litigant seeks out funding, a funder is unlikely to fall within this statute
Usury

• Charging interest at a rate that exceeds a maximum rate provided by law for the particular category of lender involved

• Usury only applicable where the underlying transaction constitutes a loan

• Litigation funding arrangements are not “loans” and not usurious under New York law
  – Obermayer Rebmann Maxwell & Hippel LLP v. West (W.D. Pa. 2015): Right to repayment contingent upon litigant’s success, arrangement is not a “loan” and usury inapplicable
  – Lynx Strategies v. Ferreira (N.Y. Sup. Ct. 2010): recovery contingent, not a loan and thus usury inapplicable
  – Dopp v. Yari, (D.N.J. 1996) (the majority of jurisdictions, including New York and California, permit collection of interest rates in excess of the legal rate when the collection is at risk and depends upon a contingency)

• Many states exempt commercial (as opposed to consumer) transactions from usury laws

• Investments in commercial litigation generally exceed the statutory limit for the application of usury laws
Work product (1/2)

• The work product doctrine protects documents “prepared in anticipation of litigation or for trial by or for another party or its representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent).” Fed. R. Civ. P. 26(b)(3)

  – A document is protected by the work product if it “can fairly be said to have been prepared . . . because of the prospect of litigation.” 8 Charles Alan Wright et al., Federal Practice & Procedure, § 2024 (2d ed. 1994)
  – Extends to “dual purpose documents” – created for both litigation and business purposes

• The core purpose of the work product doctrine is to protect the integrity of the adversarial process – eliminate unfair advantage by prying into adversary’s strategy. See Hickman v. Taylor, 329 U.S. 495, 516 (1947)

• A party seeking financing often discloses work product to the potential financier, usually under an NDA

• Broader and harder to waive than attorney-client privilege but can be overcome by showing of necessity
Work product (2/2)

- Courts have extended the work product “umbrella” to litigation finance providers, and have protected from disclosure to adversaries work product shared with litigation financiers.

- Parties obtain litigation funding to assist with litigation. Thus, the funding agreement and communications between the funder and the litigant clearly are “prepared in anticipation of litigation.”

- Every court to address the issue agrees that the work product protection applies
  - Miller UK Ltd. v., Caterpillar Inc., (N.D. Ill. Jan. 6, 2014): Work product protection applies to documents shared with funders, provided reasonable protective measures (such as an NDA) are in place
Attorney-client privilege

• Requires that a communication made between privileged persons in confidence for the purpose of obtaining or providing legal assistance for the client remain confidential

• Applicable rules: ABA Model Rule 1.6; NY CPLR § 4503.

• Sacrosanct but can be waived
  – Unlike the work-product doctrine, which is waived only when information is shared with an adversary, disclosure to any third party generally waives the attorney-client privilege, unless an exception applies

• Common interest exception may establish a non-waiver
  – Separately represented parties with a common legal interest may communicate directly with one another to advance their shared interest without waiving the attorney-client privilege.

• Frequent application of common interest: “Joint defense” agreements; Communications with insurers; M&A due diligence; Disclosure to auditors

• As a practical matter, funders may simply avoid privileged materials and instead rely on outside counsel and publicly accessible materials and information
Common interest exception to waiver of A/C privilege (1/2)

• There is a diversity of opinion on the application of the common interest exception to waiver of the attorney-client privilege in the context of litigation funding.

• One view: litigation funding agreements and communications are protected by the attorney-client privilege and common interest doctrine.
  – Walker Digital, LLC v. Google Inc., (D. Del. Feb. 12, 2013): Common interest between the claimant and funder protected privileged communications Id. at *1
  – Rembrandt Techs., L.P. v. Harris Corp. (Del. Super. Ct. Feb. 12, 2009): Reached the same conclusion as to communications between a patentee and patent consultants that shared an interest in the patentee’s successful assertion of its patent claims.
  – In re: Int’l Oil Trading Co., LLC, (S.D. Fla. Bankr. Apr. 28, 2016): “The information exchanged between the parties was for the limited purpose of assisting in their common cause, which was to propound litigation to collect on a claim.”

• Key question is not whether both parties’ legal interests are at stake in the lawsuit, but instead whether both parties’ interests relate to the outcome of that litigation.
  – Waste Mgmt., Inc. v. Int’l Surplus Lines Ins. Co., 579 N.E.2d 322, 328 (Ill. 1991) (holding that “both insurers and insureds had a common interest either in defeating or settling the claim against insureds.”).

Common interest exception to waiver of A/C privilege (2/2)

• Other view: No common interest protection because the funder’s interest is commercial rather than legal
  – Miller UK v. Caterpillar, (N.D. Ill. Jan. 6, 2014): A shared rooting interest in the ‘successful outcome of a case’… is not a common legal interest…. there was no legal planning with third party funders to insure compliance with the law, litigation was not to be averted, as it was well underway, and Miller was looking for money from prospective funders, not legal advice or litigation strategies.” But while A/C privilege was waived, work product protection applied to documents shared with funders pursuant to NDA.
  – Leader Tech v. Facebook, 719 F. Supp. 2d 373 (D. Del. 2010): The court, in making numerous discovery rulings, stated that the common interest exception did not apply to privileged information that was provided to a funder. There was no common interest agreement or non-disclosure agreement in place. Ultimately materials were inadmissible.
Confidentiality

• ABA Model Rule 1.6(a): “A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent…”

• Confidential information defined more narrowly by states: “Information that is a) privileged or b) likely to be embarrassing or detrimental to the client or c) information that a client has requested be kept confidential”

• Counsel needs informed, written consent from client before disclosing confidential information to any third party, including a litigation funder

• No evidentiary privilege is created by the rule
Potential conflicts of interest

- Attorney would be subject to conflict of interest when working with a third-party funder if
  - S/he participates directly in or benefits financially from a litigation financing transaction between the client and funder, as opposed to simply advising the client in connection with the transaction
    - Rare situation. Disclosure and consent may be prudent
  - S/he has an attorney/client relationship with the litigation financier. Model Rule 1.7
    - Standard conflicts analysis; Disclosure and written waiver may be prudent
  - S/he receives a referral fee from litigation financier
    - Rare situation; Obtain written consent from client. Model Rule 1.7(a)(2) and see Assoc. Bar City of New York, Formal Opinion 2011-2, Third Party Litigation Financing, n 16.

- No conflict of interest
  - Model Rule 1.8(e) relating to financial assistance to clients: No implication when a litigation financier is involved, as opposed to attorney providing the assistance
  - Model Rule 1.8(i) relating to the acquisition of an interest in the client’s cause of action; Not implicated when a litigation financier is involved
  - Contract between client and funder provides for payment to funder and attorney before client
    - No ethical issue. ABA: “Simply paying a portion of the proceeds of a judgment or settlement to a [litigation funder] holding a valid lien does not create a conflict of interest. A lawyer is required to deliver to a client or third party any funds in which the client or third party has an interest.”
    - Common arrangement in attorney/client relationship
Control of counsel, strategy & settlement

- Commercial litigation funders do not control litigation strategy or settlement
  - A client may contract with a litigation funder to restrict his/her ability to discharge counsel without funder’s consent. Charge Injection Technologies, Inc. v. E.I DuPont de Nemours & Co., (Del. Super. Ct. Mar. 9, 2016)
  - However, contract between client and attorney giving the latter control over settlement is not enforceable
  - There are often multiple parties involved in settlement decisions – insurers, debt holders, minority shareholders, etc

- Client can delegate that authority to a third party according to the ABA:
  - “There would seem to be no reason, as a matter of contract law, to regard these contractual provisions as unenforceable, absent some facts establishing a defense such as duress or unconscionability.”
  - “The presence of [a litigation funder] is not different in kind from the other factors that are part of virtually any decision to settle; thus, they do not present distinctive ethical issues beyond the duty of competence and the client’s authority to make settlement decisions.”

- Extreme case where funder has complete control over strategy and settlement, particularly when accompanied by other misconduct, may support a finding that a contract is champertous in certain states, e.g., Florida, Minnesota.
Independent judgment

- Model Rule 5.4(c): “A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services to another to direct or regulate the lawyer’s professional judgment in rendering such legal services.”
  - In a contract between the client and a funder, the client and not the funder pays the lawyer
  - Presence of a litigation funder does not change the lawyer’s duty to give client his or her best judgment
  - A delegation of the final decision on settlement to a litigation funder or other third party does not affect this duty: client always has the final decision on settlement, including the decision to delegate that authority to a third party. Charge Injection Technologies, Inc. v. E.I DuPont de Nemours & Co., (Del. Super. Ct. Mar. 9, 2016)
  - Relationship between litigation financier and client may be less intrusive than relationship with insurer, because financier typically does not have the right to decide settlement
Competent Representation

• Rule: 1.1

• Informing a client concerning litigation funding generally and referring a client to a specific funder has been approved by numerous state and local bar associations
  – Arizona, Florida, Maryland, Nevada, New Jersey, New York, South Carolina, etc.
  – New York City, Philadelphia, etc.

• There is no explicit duty to advise a client that litigation funding may be available. See Christine Simmons, *Judge Declines to Hold Firm Liable for Client’s Financing*, NYLJ, January 8, 2013 (no duty under Rule 1.1 to advise client receiving funding unless specifically within scope of representation).

• However, the majority of surveyed clients and attorneys agree that funding should be part of every client conversation (source: 2016 Litigation Finance Survey)
Practical application
Process, criteria, considerations
The role of the funder?

- Funders act as passive providers of finance
- No change to attorney/client relationship
  - Litigation finance provider has no control over litigation strategy or settlement decisions
- Consideration of privileged information
  - Parties execute NDA before any substantive discussions
  - Good case law in key jurisdictions confirming work product protection applies to funder communications and documents
  - A good litigation funder will be vigilant in managing relationship to avoid risking waiver of protected communications
- Reporting requirements
  - Financier typically requires regular reporting of significant case developments
  - May offer case-related advice but have no decision-making authority
Investment process

1. Initial review
   • NDA
   • Background documents reviewed

2. Diligence
   • Discussion of merits and economics
   • Term sheet offered by funder

3. Investment
   • Definitive documentation

4. Reporting
   • Funder often requires regular reporting of significant
Matters suited to financing: Criteria

- Meritorious commercial business-to-business disputes
  - Contract
  - Fraud
  - Fiduciary duty
  - Securities
  - Antitrust
  - IP
  - International arbitration
  - Insolvency
  - Other commercial claims

- Investment need that is matched to diligence required

- Damages sufficient to support return for client, lawyers and funder
Criteria for diligencing funders

• To understand the historical track record and financial capacity of a potential provider of litigation finance, lawyers should ask
  – How much money has it made? Across how many and what kind of investments? Over what period of time?
  – How much actual cash does it have invested in comparable litigation today?
  – How much available capital does it have to invest?
  – How reliable and certain are the sources of that capital? Is it legally committed?
  – What is its investment period?
  – Who are the capital sources? (Investors’ identities and the terms of the investment agreements)
  – What happens if they do not provide capital when desired?

• Given the duration of commercial litigation and arbitration, it is extremely important to identify a funder that will have sufficient capital to commit without time constraints or limitations
Code of conduct

• There is no code of conduct for US litigation funders

• In the UK, Burford is a signatory to the Civil Justice Council Working Party on Third Party Funding’s Code of Conduct, which covers
  – Clarity on promotional material
  – Clarity on confidentiality
  – Need for counterparties to be independently advised on litigation funding agreements
  – Requirement for litigation funders to be adequately resourced in terms of capital
  – Defined standards of fairness in relation to disputes that might arise between funders and their counterparties, especially around settlements and terminations
Questions?
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The role of the expert in price review arbitrations

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1. Introduction

This chapter discusses the role of the economic expert acting as a party-appointed expert witness in price review arbitrations arising from long-term natural gas supply contracts in continental Europe. We distinguish this role from testimony that may be provided by other types of expert (eg, legal expertise, which may be required if specific points of applicable law arise) and from the role of an expert appointed by the tribunal to help it in its deliberations (although much of what we say here will also be relevant to that function).

Nonetheless, a more accurate title might refer to the ‘roles’ rather than the ‘role’ of the expert. As we explain below, typically, economic testimony in price review arbitrations covers a wide range of issues, depending on the facts of the case and the price review clause itself. Therefore, the role of the expert may involve discussion and analysis of matters such as:

• market trends, using standard economic tools (eg, analysis of price trends, market concentration, barriers to entry and other factors affecting competition);
• regulatory changes (eg, developments promoting gas-to-gas competition);
• pricing, value and profitability (eg, by comparison of the price of gas under the contract at issue with prices of gas from other sources; by calculating the value of the gas in comparison with competing fuels; or by performing calculations of profitability derived from end-user price data).

In addition, the applicable law affects the role of the expert in a number of ways, including the extent to which the tribunal will be interested in the subjective intent of the parties and potentially in claims of trade practice that might be used to support some elements of contractual interpretation.

Therefore, the expert has many possible roles, which may require the use of a wide range of skills, types of evidence and analytical methodologies. The expert may be asked to act as any of the following:

• competition economist, with specialist skills in the study of industrial organisation and the application of economic theory to the analysis of markets;

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1 Whether piped gas or liquefied natural gas (LNG).
• regulatory economist, with expertise in understanding the development of economic regulation and its impact on gas markets;
• accountant, with the expertise to understand company accounts to establish, for example, whether gas is being sold profitably at the current price levels or (where there is a hardship clause in the contract) whether either the buyer or the seller is suffering ‘hardship’ within the definition;
• statistical expert, to undertake appropriate analysis of data on the market, including potentially large and complex data sets concerning pricing (see later discussion). The expert may need to perform relatively sophisticated analysis (e.g., assessing impact of changes on value while controlling for short-term factors such as weather);
• local market expert, to provide detailed local knowledge on pricing, energy use, data sources, regulatory history (which in some cases can be complex and obscure); and
• industry expert, to provide knowledge of industry practice, both current and at the time the contract was agreed.

Indeed, the set of roles is wide enough that it is quite common in our experience for one or both parties to use several experts, since often no individual will have expertise in all the required areas.

Lastly, as in other proceedings, the basic task of the expert or experts is to assist the tribunal in its role by providing clear, non-technical explanations of their analyses.

As the above may suggest, the role of the expert in price review arbitrations can be different from that in other international arbitration proceedings. It is our experience that the role of the expert can be central in price reviews. The expert witness often provides the majority of the testimony, whether measured in terms of the volume of written matter, the time spent in oral testimony or the focus of legal submissions. Factual evidence, if any, may be limited to short accounts of the negotiations that preceded the request for arbitration (since a party may wish to establish that it has followed the contractually required procedures and acted in good faith). To put this in perspective, we often see no more than 10 or 20 pages of factual testimony but several hundred pages of expert testimony, and legal pleadings often largely focus on the content of the expert reports.

Typically, the structure of expert testimony covers three or four areas:
• Economic and financial principles underlying the pricing and related arrangements – commonly, expert testimony is used to set out the relevant economic and financial principles that underlie the pricing arrangements, because it is not possible to discuss changes to those arrangements without a clear understanding of how they currently work. Explanations may cover both the pricing formula used, and important non-price terms such as the ‘take-or-pay’ mechanism.

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2 These comments apply equally to commercial litigation conducted in national courts.
3 Lest this be thought self-serving coming from two experts, we should add that it reflects the views of various international arbitration lawyers with whom we have worked.
• Analysis of ‘trigger’ – most price review clauses specify certain criteria that must be satisfied in order to justify a price revision (the ‘trigger criteria’). Most often, the trigger involves changes in economic or market circumstances that meet certain criteria (e.g., “affecting the value of gas in the Buyer’s market”).

• Analysis of ‘adjustment’ – if the tribunal finds that the criteria for triggering a review have been met, it must determine whether an adjustment to the existing pricing arrangements is justified and, if so, what adjustment is most appropriate.

• Other areas – these include providing testimony where one of the parties claims that one or more clauses of the contract are anticompetitive, or seeks to invoke a hardship clause. We have seen instances where parties suggest that pricing arrangements in existing long-term contracts are in themselves an abuse of a dominant position, or that the refusal to agree to a price reduction is an abuse.

The second and third points above (trigger and adjustment) reflect the typical structure of price review clauses.4

The rest of this chapter follows the structure described above.

2. **The expert’s role in setting out the economic and financial principles and context**

In order to understand how price review clauses generally work (in economic terms), one must first understand at high level the principles behind gas pricing in long-term gas sales agreements. Indeed, pricing arrangements and price review clauses are sometimes said to go hand in hand.

Also, to understand the issues that arise in most price reviews, one must have some knowledge of developments in European natural gas markets. Typically, therefore, the expert will need to include in his or her testimony some or all of the following:

• the mechanism of pricing in long-term gas sales agreements;
• the origins of these pricing mechanisms, including (but not limited to) concepts such as:
  • the ‘equivalence principle’ (often referred to by the German *Anlegbarkeitsprinzip*) and net-back pricing;
  • benchmarks based on comparison with border prices;
  • the balance of risk in traditional long-term contracts, including the role of take-or-pay clauses under which the buyer takes on the bulk of the volume risk; and
• recent and ongoing market developments (both regulatory and commercial developments may be relevant).

---

4 We note that in our experience this two-part (trigger and adjustment) structure is one of the few points common to most price review clauses, though not all. In most respects, price review clauses vary widely. Some writers have suggested a ‘typical’ or canonical price review clause, or claim that price review clauses form a ‘single family’. The reality is more complex – as one colleague has said: “The ‘family of price review clauses’ is like the ‘family of dogs’ – there are common features across the family, but one clause need not look anything like another.”
2.1 **Pricing in long-term gas sales agreements**

The pricing formulae in long-term gas sales agreements look complex. However, conceptually, the formulae usually represent a relatively simple underlying relationship between the contract price and a ‘basket’ of prices of alternative fuels (usually some or all of crude oil, refined oil products such as gasoil and fuel oil, and coal).\(^5\) There is often a base price, with an indexation element that tracks this basket of other fuels. This is illustrated graphically in Figure 1.

**Figure 1: Illustrative relationship between contract price and basket of other fuels**

![Illustrative relationship between contract price and basket of other fuels](image)

As Figure 1 shows, the price of gas is set at the base price on the day that the pricing arrangements go into operation. It then moves with the basket of alternative fuels: if the price of the basket increases (positive change in value), the price of gas increases, and vice versa.

There have been two general approaches to determining pricing formulae reflected in most long-term contracts. One common approach is based on the difference between an estimate, or proxy, for the end-user price or value of gas in the buyer’s market and an assumed gross margin – that is, allowing for reasonable costs and profit:

\[
\text{Contract price} = [\text{estimated end-user price/value}] - [\text{assumed gross margin}]
\]

If the buyer is able to resell the gas in line with the estimated end-user price/value, this formulation will give it the intended margin.

Historically, under this approach the estimated end-user price/value was derived or expressed as the price of a basket of alternative fuels. The composition of that basket...
basket (ie, the relative weights of the different fuels in it) reflected the composition of the buyer's market. Different sectors of that market were linked to different alternative fuels. In other cases, the price is derived by negotiation, either with or without explicit reference to end-user prices. In such cases the choice of basket and of weights in the basket will also be a matter of negotiation.\(^6\)

Another widely used approach to deriving the pricing formula has been by comparison with other upstream contracts. The underlying commercial logic is that setting a price that is comparable to that in other contracts should allow the buyer to remain competitive, and also reassure the seller that it is not selling at too low a price.

These two approaches may produce price formulae that have the same mathematical form, despite their different bases. However, they are shown in different ways in different price review clauses, which may make reference to one or both as the relevant criterion.

With the development of gas hub trading, a third approach to pricing gas is becoming increasingly relevant: indexation to price levels at EU trading hubs such as the NBP (National Balancing Point) in the United Kingdom or the TFF (Title Transfer Facility) in the Netherlands.

2.2 Take-or-pay clauses

Long-term gas sales agreements often include take-or-pay arrangements. Despite the name, this does not usually mean that if the buyer does not take the minimum volume under the contract it is obliged to pay for gas that it does not receive. Rather, it is better to think of such clauses working more like banking arrangements. Specifically, if less than the minimum volume is taken, the buyer must pay in advance part or all of the contract price for the gas not taken. In return for this, the volume of gas is 'banked', and can later be called upon by the buyer (in return for a payment of the rest of the contract price, if only part-payment was made in advance). Therefore, essentially, the take-or-pay payment gives the buyer the right to take the relevant volume of gas later. However, in our experience, there is typically a time limit requiring banked gas to be taken within a specified number of years. Any gas not removed from the bank at the end of this period would be lost. Moreover, there is obviously a cost to advance payment. Depending on the circumstances, the take-or-pay arrangements may be either advantageous or burdensome to the buyer.

2.3 Recent and ongoing market developments

As experts, we are often asked to analyse recent or ongoing market developments. This is almost always relevant background for consideration of the trigger criteria,\(^7\) but can also be useful to a tribunal when considering a price adjustment, especially if the contract states that any such adjustment must allow the buyer the ability to sell the gas in a downstream market. Typically, expert testimony will cover a number of kinds of ongoing market developments including:

---

\(^6\) In reality, it is likely that many elements of a contract formula will reflect the results of negotiation, even if the starting point was an analysis of end-user prices.

\(^7\) In relation to whether a specific event has occurred, but also in relation to whether an event was foreseeable, as discussed below.
• European gas market liberalisation – for example, relevant EU and national legislation.
• The effects of liberalisation – for example, the development of hub trading and the corresponding increase in liquidity of hub markets.
• Market events – for example, economic downturns, the decoupling of oil and gas prices, the development of renewable energy, and the possible impact of increasing LNG and shale gas production.

3. Expert testimony concerning ‘trigger’

It is common (though not universal) for long-term gas sales agreements to specify various criteria that must be met in order to trigger a price review (usually referred to as ‘trigger criteria’). The specific criteria vary between different price review clauses, but typically they refer to changes in certain economic, financial or commercial circumstances. In addition, there are timing criteria: typically, a price review can occur only on a specified date (often every three years from a specified starting date, although in some contracts this requirement is softened by allowing each party one or more ‘jokers’ – ie, the right to request one or more price reviews outside the normal schedule).

Where the trigger criteria require there to have been “changes in [economic] circumstances” (or similar language), generally, these changes must meet certain additional criteria. These criteria are quite varied, but typically involve various qualifiers on the kind of change that can trigger a price review. For example, they must be “significant”, “expected to be long-lasting”, “beyond the control of the parties”, “not reasonably foreseeable”, as well as meet certain geographical criteria, and so on.

The changes are often required to have had an effect on “the value of gas” or a similar concept. Again, the specifics of this criterion vary very significantly. In some cases, the ‘value concept’ is not defined; in others it is specified relatively clearly (eg, by reference to the prices paid in comparable contracts or by reference to competing energies, if relevant).

In general, these criteria must be assessed by comparing circumstances at two specified dates:

• a start date, which is commonly the date of signing of the contract or of the last price revision; and
• an end date, which is commonly the date on which a formal request for the price review was made by one party to the other (the ‘trigger date’).

This period is sometimes referred to as the ‘trigger period’ or the ‘comparison period’, or simply the ‘relevant period’.

Therefore, the expert’s role in assessing whether the trigger criteria have been met often involves (conceptually) two elements: describing the alleged changes in economic circumstances and assessing them against the specified criteria. Generally, this requires the expert to develop both qualitative and quantitative evidence. We illustrate with two examples. The first is a relatively straightforward change that is typical for a traditional price review (in contrast to a review that focuses on the impact of liberalisation). The second relates to liberalisation and gas-to-gas competition.
Example 1: A ‘traditional’ price review

Suppose that the government of the country where the gas is delivered and sold (the buyer’s home market) increases/decreases the excise duty (ie, tax) on a certain competing fuel,8 say fuel oil. Suppose also that this would be a valid trigger for a price review under the price review clause in question, which defined ‘value’ by reference to competing fuels. First, the expert would need to document the change in excise duty (by reference to official publications), and show by how much it affected the price of fuel oil, in particular in applications where it was a competing fuel for natural gas.

Second, the expert would need to show that the change affected the value of gas, and estimate by how much it did so. In brief, the likely effect would be that an increase in duty would make it possible for the buyer to raise the price that it charged for natural gas to those customers for whom fuel oil was the main alternative to natural gas, since the increase in duty would make that alternative more expensive. Conversely, a decrease in duty would be likely to lead to a lowering of the price charged to those customers. In that case, the expert might need to:9

- document that fuel oil was indeed a competing fuel for natural gas, in the market in question, at the relevant point(s) in time;
- estimate the amount or proportion of sales of natural gas from the contract under review that could be considered to be sold in competition with fuel oil, at the relevant point(s) in time;
- show that at the beginning of the period under review, natural gas sold in competition with fuel oil was priced at a level to make it competitive with fuel oil;
- calculate by how much the price should change in those circumstances, taking into account various technical parameters (eg, the relative efficiencies of appliances using natural gas and using fuel oil, in various applications); and
- calculate the average impact on the price that the buyer could obtain for its gas (given that this change affects only part of its market).

Depending on how the ‘value of gas’ is defined in the relevant contractual provisions, the result of this exercise might be considered to be the impact on the value of gas (it would not be so if, eg, the contract required the value of gas to be assessed on the basis of comparison with the price of gas in other import contracts and not at end-user level).

8 Historically, gas pricing in contracts with end users in continental Europe was often derived by considering the price of alternative fuels that the customer could use for the same purpose (eg, a household might choose to use gasoil for heating if it did not use natural gas). In this context, these were referred to as ‘competing fuels’.

9 We do not claim the following list to be either necessary or sufficient. The specific nature of what is appropriate expert evidence will depend on the factual details of the matter in question, and the specific contractual requirements.
Example 2: Review driven by market liberalisation and gas-to-gas competition

Suppose the buyer seeks a price review on the grounds that EU and national legislation that have liberalised the gas market, and this has led to competition from other suppliers that has pushed down the price that it can obtain for its gas (and suppose again that this would be a valid trigger under the price review clause). In this case, the expert might need to:

1. describe and document the legislative and regulatory changes that have liberalised the market;
2. describe and provide evidence of market responses to these changes. This might involve, for example, evidence concerning the entry of new competitors or changes in pricing that can be linked to gas-to-gas competition. The types of evidence used could include data of the sort commonly used in competition economics (e.g., market shares, changes in pricing compared to a competitive benchmark), as well as more business economics types of documentation such as market commentary from trade press, broker notes, and so on. National regulators and academic economists may also prove useful sources; and
3. demonstrate that the market response has affected the value of gas in the relevant market. Depending on how the contract defines ‘value of gas’, this could involve, for example, analysis of import and/or end-user prices, to estimate how they have changed relative to relevant benchmarks such as the price of oil or the price of gas at trading hubs.

In our experience in recent price reviews, debates about liberalisation vary significantly depending on the specific countries and time periods under discussion. The pace of gas market liberalisation across the European Union also varies significantly. In some member states gas markets are highly liberalised, while in others liberalisation remains more a theoretical possibility than a significant factor affecting the market. Therefore, in some cases there may be material debates on the extent to which the liberalisation is sufficient to warrant a price review. In other cases, the effects of liberalisation may be clearer, but experts may disagree on issues of timing and whether the start of competition fell within the contractually relevant time period. In yet other cases, where the price review clause and/or applicable law exclude changes that were reasonably foreseeable at the beginning of the relevant time period, there may be discussion on the extent to which the changes attributed to liberalisation were foreseeable. The types of evidence that the expert may rely on, and the analyses he performs, can vary considerably. In some cases the expert will rely significantly on personal knowledge, particularly in markets that historically have been less transparent. In other cases, the expert may rely significantly on public documents (e.g., legislation, regulations, official publications, as well as trade and business press, analyst

As in the previous example, we do not claim the following list to be either necessary or sufficient.
reports from banks). The expert may use a range of different data sources, including:

- data from public sources (e.g., EU data, data from national statistical agencies, data from energy regulators);
- data purchased from survey companies,\(^\text{11}\) which may be produced specifically for the expert or be generally available; and
- the buyer’s internal data on the prices that it achieves as a gas marketer.

In the last case, there are typically disagreements between the parties over the disclosure of data, and the expert must be ready to deal with data at short notice (if disagreements over data provision have led to delays in disclosure, as is often the case) and under potentially burdensome confidentiality requirements. This is particularly so if the data can be accessed and worked on only in a secure data room. The expert may need to have a team able to use business software packages such as SAP, and to process large datasets, both in terms of data handling and in terms of undertaking numerical and statistical analyses.

### 4. Expert testimony concerning price adjustment

In our experience, the variation between price review clauses is particularly marked with regard to the contractual criteria that apply to a price adjustment. Therefore, it is likely that the expert will be asked to provide an opinion on a range of relevant areas, depending on what is specified in the contract with respect to the adjustment.

The adjustment criteria may be explicitly linked to the trigger criteria (e.g., “adjust to reflect the changes”). Alternatively, the clause may specify other criteria for the price adjustment, even if they are not (explicitly) required for trigger. For example, some clauses require any adjustment to take into account a comparison between the contract price and the pricing in other comparable long-term gas supply contracts, even if the trigger does not make any reference to other such contracts.

Some price review clauses also specify that the adjustment should be such that the buyer is “able to market” the gas “economically”, subject to certain safeguards for the seller: such requirements may be argued to mean that the price should allow the buyer to sell the gas, cover its costs and earn some kind of a net margin, provided that the buyer acts and has acted efficiently and prudently in its marketing and operations.

Some contracts also exclude certain changes from the scope of the price review clause, so that the buyer is explicitly required to bear the corresponding risk. Examples are pricing clauses that exclude taxes or exclude changes to the taxation regime.

There are also some basically technical issues that arise, depending on what the claimant (whether buyer or seller) is looking to change.

For example, the claimant may wish to reset only the price level in the contract, but not to change the indexation mechanism. This would involve only a change to the $P_0$ parameter in the price formula, as illustrated in Figure 2.

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\(^{11}\) In our experience, one or both parties may commission surveys to obtain data on pricing from large customers.
Alternatively or in addition, the claimant may wish to change the ‘slope’ in the price formula (i.e., the percentage of the prevailing oil price that sets the price), so that future changes in the oil price have a lesser or greater impact on the contract price than they would under the pre-award formula. The expert may need to explain carefully the economic significance of a change in slope.
Alternatively, the claimant may wish to change what the price is indexed to (though in some cases the price review clause explicitly forbids this). In particular, in some recent cases the claimant has sought to introduce a new element of indexation to the price of gas being traded on commodity exchanges (‘gas trading hubs’, giving rise to ‘hub indexation’).

The introduction of hub indexation is more complex to evaluate and calibrate for the contract than the other adjustments described above. The price of gas on a hub is the price for a basic contract involving the delivery of the same amount of gas each day over a defined time period. In contrast, a typical long-term import contract gives the buyer (and, to a much lesser extent, the seller) a certain amount of flexibility on the amount of gas that it takes over various timeframes, ranging from a day to a year. Depending on the details of the proposal, the price of gas in a hub-indexed contract may therefore need to reflect this difference, which may require complex and potentially challenging calculations.

5. Expert testimony in other areas
In our experience, there are often specific individual features of a contract or of a dispute that require additional expert evidence. These include a range of competition issues, and analysis related to the application of specific contractual clauses, such as hardship clauses.

5.1 Competition issues
It is open to either or both parties to raise additional legal points in the context of arbitrations. We have seen both buyers and sellers introduce competition law-based arguments that require input from economic experts. These arguments may involve a claim that part of the contract itself is anticompetitive, breaching Article 101 of the Treaty of the Functioning of the European Union (TFEU) or the national equivalent legislation,12 or that some aspect of the contract represents an abuse of a dominant position (eg, on grounds of excessive pricing), contrary to Article 102 of the TFEU or the national equivalent legislation.

In either case, usually the expert is required to provide an opinion on the relevant product and geographical market definitions within which the market shares of the seller and/or buyer should be measured, and to calculate the relevant market shares. Such market shares are potentially important either for the purpose of establishing whether the contract in question is entitled to an exemption under Article 101 of the TFEU, or to help determine whether the buyer or seller was dominant at the relevant point in time, based on standard legal criteria for dominance.

5.2 Hardship clauses
Hardship clauses are clauses that provide some form of relief if one party is suffering from ‘hardship’ (a concept which may be rather vaguely defined). Some of the long-

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12 To clarify, the claims we have seen are not related to allegations of collusive/cartel-like behaviour, but to ‘vertical issues’ – for example, resale restrictions (so-called ‘destination clauses’ that limit the ability of the buyer to resell the gas outside its own market area).
term gas sales agreements with which we are familiar include a hardship clause in addition to the price review clause. These clauses are examined elsewhere in this book.

If a party is claiming the benefit of a hardship clause, the expert’s role is likely to include an analysis of the relevant financial evidence to reach a view on whether the relevant party is, in fact, suffering hardship, within the definition of the clause. This may involve a rigorous accounting analysis to assess the link between the profit/loss shown in accounts and the underlying economics. For example, it may be due to a provision in the accounts, reflecting an expectation as to future losses, rather than actual operational loss in the period in question. Conversely, an accounting profit may reflect the outcome of financial hedging, rather than the effect of sales to consumers.

6. Some process issues
Lastly, we provide a few comments from an expert’s perspective on the process issues that arise in price review arbitrations.

First, we note the obvious: independence is central to the role of the expert. As in other areas, experts should not become advocates for the party that has appointed them.

Second, in our experience the key points of disagreement between experts can be relatively narrow. In some cases, expert reports appear to provide very different views, but the underlying difference arises from the legal view of the contract that they have been instructed to take by counsel. In other cases, we have seen expert reports where there was close agreement on the majority of the facts and analysis. In such instances, it can be useful for the expert to explain to the tribunal the areas of agreement, so as to help focus attention on the remaining areas in dispute. Tribunals often seek to achieve further progress on those areas through techniques such as requesting a joint report from the experts, or the use of witness conferencing.
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This third issue of *Asian Dispute Review* for 2015 covers a wide range of issues relating to the practice of arbitration in Asia. We commence with an article by Neil Kaplan QC and Olga Boltenko, who survey the potential of mock arbitrations or ‘in-house mini trials’ to help prepare for or defend an arbitration claim. Next, Professor Neil Andrews and Dr Fan Yang provide an overview of English arbitration law by reference to both English and Hong Kong law, which is relevant to most common law jurisdictions in Asia. Following this article, Michael Dunmore addresses the use of emergency arbitration provisions with a brief survey of the position in some major Asian jurisdictions, Man Sing Yeung describes the 2015 CIETAC Arbitration Rules and its *Guidelines on Evidence*, and Mauro Rubino-Sammartano and Shahla Ali explore internal review processes under the rules of international arbitral institutions in the second part of their article on whether internal appellate proceedings in arbitration have reached Asia. The In-House Counsel Focus article is by John Molloy on the consequences of expert evidence. This is based on an edited text of the 9th Annual Winnie Whittaker Memorial Lecture delivered at the HKIAC.

A case note by Sheila Ahuja and Chantal du Toit deals with the Hong Kong High Court decision in *Z v A*, which denied the challenge to an arbitral tribunal’s jurisdiction brought under Hong Kong’s equivalent of article 16 of the Model Law. Two book reviews follow, one by Neil Kaplan QC on *Construction Arbitration in Hong Kong: A Practical Guide* and the other by Nils Eliasson on *Enforcement of Investment Treaty Awards: A Global Guide*.

Finally, we take this opportunity to thank Michal Čáp for his generous and extremely helpful contribution as Editorial Assistant to the *Asian Dispute Review*. This is the last issue he will be working on before returning to the Czech Republic. We wish him well and are grateful for the considerable support he has given to this publication.
A Secret Tool for Winning an Arbitration Case

Neil Kaplan CBE QC SBS & Olga Boltenko

This article describes a known but yet remarkably neglected tool to prepare for and defend an arbitration case successfully: a mock arbitration, also known as an ‘in-house mini trial’. Mock arbitration is arguably rooted in a US litigation tradition of mock jury trials. This tradition is now being applied to arbitration practice by the most sophisticated counsel in the field. The pros and cons of this tool are explored and the authors offer a comprehensive guide to the use of mock arbitration in practice.

Introduction

What is experience? Is it any more than having been around long enough to have seen most things? As the Bible says, “What has been will be again, what has been done will be done again; there is nothing new under the sun”. A precedent can be found for most human situations; so too with arbitration and litigation.

Are American litigants leading the way?

There are many aspects of the United States legal system that are well known and unacceptable to an English, Hong Kong or Russian lawyer. The excesses of US-qualified counsel over document production, for example, would be anathema to most national legal systems. Indeed, even US judges themselves are known to despair over the painful US brand of discovery. In 1989, Wayne E Alley, an Oklahoma judge, issued a procedural order dealing with document production issues in which he said:

“[i]f there is a hell to which disputatious, uncivil, vituperative lawyers go, let it be one in which the damned are eternally locked in discovery disputes with other lawyers of equally repugnant attributes.”

In other areas, however, American-style precautions seem rather sensible. The Americans prefer not to leave too much to chance in dispute resolution and this approach proves successful on many occasions. For decades now, US litigants have been using mock jury trials. It is well known that juries
ARBITRATION IN ASIA

are used in the US for the determination of a wide range of civil disputes as well as for criminal trials. The purpose of a mock jury trial is to predict how an actual jury would react to a case. The mock jury is selected from the same community as that from which the actual jury would be selected. Counsel present their case to the mock jury and observe its deliberations and the processes used in reaching its decision(s).

The purpose of a mock jury trial is to predict how an actual jury would react to a case. The mock jury is selected from the same community as that from which the actual jury would be selected. Counsel present their case to the mock jury and observe its deliberations and the processes used in reaching its decision(s).

From mock jurors in the US to civil litigation and international arbitration

In civil cases, particularly in the US, it is the authors’ understanding that practitioners will often try out their arguments before a mock judge (who may in fact be a retired judge). In relation to arbitration cases, Lucy Reed, in her Kaplan Lecture delivered in Hong Kong in December 2012 and entitled Tribunal Decision-Making: Art, Science or Sport?, suggested that, in order to convince an arbitrator, one must

“focus not so much on what may go on in an arbitrator’s head but more on how much can fit in an arbitrator’s head”.

None of this is new: as Quintilian said in the first century AD/CE:

“we must not always burden the judge with all the arguments we have discovered, since by so doing we shall at once bore him and render him less inclined to believe us”.

Presenting a complex case to a retired judge or a practising arbitrator at a mock arbitration allows counsel to assess whether the actual tribunal would be able to ‘fit’ the case in its collective head. In 2009, Amy Rothstein, a US-based arbitration practitioner, was one of the first practitioners to speak openly about mock arbitrations as useful tools for preparing an arbitration case. She connected the practice of mock arbitrations with the very US-focused practice of mock jury trials. She wrote that:

“the purpose of mock arbitrations is similar to that of mock trials: to obtain from a hypothetical adjudicator a likely decision and underlying reasoning, based on a presentation of the evidence and arguments that counsel expect to offer.”

Arbitration is lagging behind these developments when it comes to the tools that arbitration practitioners use (or at least those of which they are aware) when selecting arbitrators or framing their arbitration strategy generally. The authors are, for example, aware of specialised firms that offer witness training services. Stepping into attorneys’ shoes, these firms explain to prospective witnesses what cross-examination is all about, how to behave, what to expect and how to react to questions coming from the panel and from opposing counsel. So far as one can tell, however, arbitration practitioners are not making use of the in-house mini trial technique to test their legal or factual positions.
In 2010, international arbitration commentators Doak Bishop and Edward Kehoe were the first to proclaim publicly that –

“the most useful scientific tool we have in preparing for an arbitration hearing is a mock arbitration panel study”.8

Then, in 2012, New York-based arbitrator Edna Sussman wrote that –

“the use of mock arbitrations to enhance the likelihood of successful outcomes in larger cases is likely to grow significantly in the coming years as those in the arbitration community become more familiar with the availability of these tools and their benefits.”9

In 2013, Dr Klaus Sachs and Dr Nicolas Wiegand added an interesting perspective to the debate, given especially that they come from a civil law background but with present experience in international arbitration.10 They state that “[m]ock arbitrations represent a nascent but palpable trend.”11

A secret to winning?
The authors agree with Edna Sussman and other leading practitioners in the field that there is no better tool with which to prepare an arbitration case than a mock arbitration before a practising arbitrator or someone who is familiar with the actual decision-making process of an arbitrator. They anticipate that in the years to come, larger law firms and other practitioners will increasingly resort to mock arbitrations in the preparation of their cases.

The structure of the mock arbitration process will certainly be adjusted in a manner commensurate with the actual arbitration and counsel’s capacity and needs. The authors predict that a typical mock arbitration case would run along the following lines.

At the outset of the mock arbitration process, the participating law firm would identify mock arbitrators with backgrounds similar to those arbitrators who sit on the actual arbitration case, or they would identify at least those who are familiar with the actual arbitrators and those who would be in the best position to assess the actual arbitrators’ views and decision-making processes.

Once the mock arbitrator(s) is/are ‘appointed’, the law firm would need to adapt and reduce its submissions so as to cover the key points at issue, thus making them suitable for a presentation before mock arbitrators. There is, of course, no need for lengthy written submissions, as these would have been prepared in the actual matter in any event. What is essential at this stage is for counsel to take the mock process seriously, so that it becomes a normal part of case preparation in appropriate cases. One or two members of the counsel team would stand in the shoes of the party against whom they act in the actual arbitration. The others would argue their client’s actual case before the mock arbitrator(s). The two teams would each prepare a concise memorandum for the mock arbitrator(s) in which they would set out the actual client’s position and that of the actual opposing party. A mock hearing would then be held before the mock arbitrator(s).

“… [F]ocus not so much on what may go on in an arbitrator’s head but more on how much can fit in an arbitrator’s head.” – Lucy Reed, Kaplan Arbitration Lecture 2012.
An interesting issue arises where the mock arbitration extends to the hearing of the witnesses. This might be an appropriate course of action in cases where witness testimony might be significant. But there are certain matters to be considered before going down this path. Drs Sachs and Wiegand remind us that there is a distinction between the US- and UK-based systems in relation to witness testimony. In the US, as mock trials are common in the court system, there is a natural progression in conducting mock arbitration hearings; it is not contrary to the bar codes for there to be contact between counsel and witnesses and the training of witnesses is common. Cross-examination in a mock arbitration would not, therefore, be objectionable. In England & Wales, however, the situation is different. Under the Code of Conduct of the Bar of England & Wales –

“a barrister must not rehearse, practise or coach a witness in relation to his evidence.”

Lawyers are, of course, allowed to familiarise witnesses with the likely procedure and the basic requirements for giving evidence, such as the need to speak slowly and to answer the question. The guiding rule is, however, that in discussions with witnesses –

“great care must be taken not to do or say anything which could be interpreted as suggesting what the witness should say, or how he or she should express himself or herself in the witness box”.

The Code of Conduct in England and Wales applies to arbitration, so that English barristers must observe those rules when appearing in international arbitration.

The Bar Standards Board (England & Wales) draws a distinction between (i) close questioning of a witness in order to present full and accurate evidence, so as to test the reliability of the evidence, and (ii) questioning with a view to encouraging the witness “to alter, massage or obscure his real recollection”; the latter is not permitted. Interestingly, the same guidance states that mock cross-examinations or rehearsals of particular lines of questioning that counsel proposes to follow are not permitted.

The position in Hong Kong is similar to that obtaining under the rules of conduct in England & Wales. While Principle 10.12 of the Law Society of Hong Kong’s guide to professional conduct permits interviewing witnesses and prospective witnesses, it is not permissible in Hong Kong to “tamper with the evidence of a witness or attempt to suborn the witness into changing his evidence.”

Thus, if English and Hong Kong barristers and solicitors are involved, it may be best to forego the mock cross-examination of witnesses, or at least to leave this to be done by a solicitor or foreign counsel not bound by the English or Hong Kong rules.

The crucial part of the mock exercise is feedback from the mock arbitrator(s) following the completion of the hearing. This feedback is, in fact, the whole point of the exercise. During the feedback session, which might conceivably take a day or two, depending on the case, the mock arbitrator(s) would comment on the merits of the case, advise counsel on their presentation techniques, recommend better ways to present the case, look into the strengths and weaknesses of the opposing party’s position, and perhaps even suggest better arguments than those presented to the mock tribunal.

Selecting the right mock arbitrator and deciding upon a mock arbitration

Just as the actual arbitration is only as good as the arbitrators whom the parties appoint, it is conceivable that the mock arbitration is only as good as the mock arbitrator(s) selected. There are several criteria to take into account in considering both of these questions.
The first criterion is the knowledge of the actual arbitrators and of their decision-making process(es), and the similarity of their backgrounds.

The second criterion is the cost of the mock exercise. For many, this criterion would come first in order of importance. Whether or not spending extra fees on a mock arbitration is justified depends on \textit{(inter alia)}:

1. the nature and the complexity of the actual arbitration case;
2. the amount(s) at stake; and
3. the importance of the case to a client.

If a law firm is defending a government in an investment arbitration commenced by a distressed investor, and the amounts claimed exceed the government’s annual case defence budget, then it is suggested that spending a bit extra on a serious mock arbitration exercise is both justified and justifiable to the client. On the other hand, if the case is before a sole arbitrator and concerns a modest breach of contract, it would admittedly be hard to convince a client to go through a full mock exercise.

The third criterion is whether the law firm has the willingness and ability to entertain a mock exercise in a serious manner. The disputes team of a law firm considering such an exercise may in fact be working flat out on tens of arbitration matters, while the disputes lawyers may not have the physical capacity to integrate a mock arbitration into their schedules.

Another issue is whether, if a mock arbitration is conducted, the costs of it can be recovered. The answer to this would depend on individual tribunals, though the authors think that most tribunals would be reluctant to allow these costs as recoverable from the losing party. The costs that a losing party has to pay must be reasonable. If that party itself used a mock tribunal, then most tribunals would be prepared to allow the costs. If, however, only the winning party did so and especially if it had deeper pockets, the authors believe that most tribunals would be reluctant to allow these costs. It must, however, follow that there would be differences in approach, depending on the legal background of the tribunal making this decision.

\textbf{Conclusion}

The advantages of the mock arbitration exercise have been admirably summarised by Drs Sach and Wiegand, who state:

“[B]eing able to discuss with professional arbitrators their thoughts and deliberation process can obviously be of enormous help to counsel in preparing for the real hearing. However, the use of mock arbitrations is also useful to give the client realistic expectations as to the outcome of the case and perhaps persuade a stubborn client to reconsider the possibility of reaching a settlement.”

The authors believe that the mock arbitration system has a real role to play in arbitration in Asia, where a growing number of new firms and individuals are engaging in the process. The ability to be able to try out the substance and presentation of arguments before a mock arbitrator experienced in the region would turn out to be an invaluable tool in case presentation in the years to come. It should be budgeted for and used in appropriate cases. It would result in better presented cases with more streamlined submissions. It would introduce into the process what has been missing for some time, namely, arbitral triage. Finally, it would help eliminate the ‘kitchen sink’ approach that so greatly bedevils international and domestic arbitration today.

Ecclesiastes 1:9.


Quintilian’s *Institutes of Oratory*, Book V, Ch 12.8. The treatise on the art of oratory by Quintilian (Marcus Fabius Quintilianus, c 35-c 100 AD/CE) is an exhaustive analysis of Roman educational practices, treasured for centuries by Western scholars. Available online at http://rhetoric.eserver.org/quintilian (accessed 18 February 2014).


Bar Standards Board (England & Wales), Section 5, *Guidance on Witness Preparation*. See also section 705(a) of the Code of Conduct of the Bar of England & Wales.

ibid, Section 12(2), n 9.

ibid, Section 5.

The *Hong Kong Solicitors’ Guide to Professional Conduct of the Law Society of Hong Kong* provides, at Chapter 10, Principle 10.12, that: “It is permissible for a solicitor acting for any party to interview and take statements from any witness or prospective witness at any stage in the proceedings, whether or not that witness has been interviewed or called as a witness by another party.” ibid, commentary.

Sachs & Wiegand, op cit (note 12 above), p 343.

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Fundamentals of International Commercial Arbitration: English and Hong Kong Developments

Professor Neil Andrews & Dr Fan Yang

This article, in addition to providing an overview of developments in English arbitration law, discusses, by reference to both English and Hong Kong law, developments in relation to anti-suit injunctions and the enforcement of international arbitral awards vacated by a court at the seat of the arbitration. The article is based on a paper given by the first author to an evening meeting of the Hong Kong Institute of Arbitrators at the Hong Kong office of Squire Patton Boggs on 22 January 2015.

Introduction
As the first author has suggested elsewhere, international commercial arbitration is supported by three pillars: (1) agreement (because arbitration presupposes that the parties positively opt into this consensual form of dispute resolution); (2) qualified autonomy (or ‘judicial minimalism’), in the sense that courts are expected to respect the capacity of the arbitral tribunal to determine (at least provisionally) its jurisdiction and for the same tribunal to apply a procedure and to reach an award largely but not absolutely unencumbered by national court interference; and (3) international (judicial) enforcement of commercial awards. English and Hong Kong developments examined in this article manifest judicial respect for all three pillars.

Part I: Overview of developments in English arbitration law
The law of arbitration in England & Wales was substantially codified by the Arbitration Act 1996 (England & Wales, Northern Ireland) (the 1996 Act), which must be read in the light of the report of the Departmental Advisory Committee on Arbitration Law (DAC).

Unlike many other nations, England did not adopt the UNCITRAL Model Law. The main deviation from the Model Law is s 69 of the 1996 Act, which permits appeals from awards (subject to the High Court’s permission) where there is alleged to have been an error of English law.
Part 1 of the 1996 Act applies where the juridical ‘seat’ of the arbitration proceedings is in England & Wales (hereinafter ‘England’) or Northern Ireland. The English Court of Appeal in *Sulamérica Cia Nacional de Seguros SA v Enesa Engenharia SA* (2012), having rejected an implied choice of the law of the underlying contract as the proper law for the arbitration agreement concerned, held that the law of the seat, England, had the closest connection with the arbitration agreement.10

The parties’ consensual autonomy is a leading feature of the 1996 Act, s 1(b) of which provides that the parties should be free to agree how their disputes are resolved, subject only to such safeguards as are necessary in the public interest. This is, however, qualified by the ‘mandatory’ provisions listed in Schedule 1 to the Act, which applies by virtue of s 4(1).11

Furthermore, the modern principles for the interpretation of written contracts in English law apply to jurisdiction and arbitration agreements, including the court’s power to recast botched text when the true intention is readily discernible.17


The High Court can hear a challenge to an award where it is alleged that the tribunal lacked jurisdiction (s 67 of the 1996 Act), or there has been a “serious irregularity affecting the tribunal, the proceedings or the award” (s 68 of the Act). Neither section 67 nor 68 can be excluded by agreement, as they are both ‘mandatory’: see Sch 1 of the Act. The House of Lords in the *Lesotho* case (2005),19 however, noted that a ‘mere’ error of fact or law within the tribunal’s jurisdiction does not justify resort to s 68.20

There can be no appeal from an English award to the High Court on a point of foreign law,21 but s 69 permits an appeal on a matter of English law,22 if the court itself gives permission. In 2006, the retention of this appellate opportunity was favoured by a majority of respondents to a survey.23 Careful wording is required to exclude s 69.24

The Privy Council, in *Associated Electric & Gas Insurance Services Ltd v European Reinsurance Co of Zurich* (2003),25 held that issue estoppel can arise in arbitration, and this will be binding on a second arbitration panel seised with a matter on a related topic between the same parties.

The UK Supreme Court, in *Dallah Real Estate & Tourism Holding Co v Pakistan* (2010),26 held that a foreign award (rendered in Paris) could not be recognised and enforced in England (under the New York Convention (1958), enacted as s 103 of the 1996 Act) because the arbitral tribunal had incorrectly determined that the Pakistan Government was a party to the relevant arbitration agreement. A French court,
Part II: Court injunctions in support of arbitration agreements and proceedings (anti-suit injunctions)

(1) England

The UK Supreme Court held, in AES Ust-Kamenogorsk Hydropower Plant LLP v Ust-Kamenogorsk Hydropower Plant (2013) (the AES case) that:28

(1) anti-suit injunctions can be granted by the courts under s 37 of the Senior Courts Act 1981 (the general power to issue injunctions);

(2) such an injunction gives effect to an implicit negative29 undertaking in any arbitration agreement that both parties will exclusively pursue arbitration for the purpose of obtaining a determination on the subject-matter of the dispute covered by the contemplated arbitration. Parties to arbitration agreements therefore implicitly undertake to refrain from litigating in the courts. The anti-suit injunction operates directly to uphold that commitment to use arbitration, to the exclusion of other forms of dispute resolution;

(3) such an injunction is conceptualised as an ordinary remedial response to a contractual breach where damages are not an adequate remedy because they would involve compensation for a wrong ‘after the horse has bolted’;

(4) there is no need to locate the court’s power to issue anti-suit injunctions as part of the internal law of arbitration (that internal law is partially codified in the 1996 Act); and.

(5) the limitations on judicial injunctions in support of pending and imminent arbitration contained in s 44 of the 1996 Act are therefore irrelevant to an application for an anti-suit injunction.

Anti-suit injunctions banished between Member States of the European Union (EU)

It has become obvious that, with regard to the topic of anti-suit relief, the common law and civilian traditions are at odds (many civil law jurisdictions have not adopted anti-suit orders).30 Matters came to a head within the EU when the European Court of Justice (ECJ), in Allianz SpA v West Tankers Inc ‘The Front Comor’ (2009)31 (the West Tankers case) held that English courts cannot issue anti-suit injunctions vis-à-vis court proceedings in Member States. This prohibition applies to all forms of anti-suit injunction where the relief is targeted at a party bringing court proceedings in a Member State. The prohibition therefore includes attempts to restrain a party to an arbitration agreement from continuing such wrongful judicial proceedings in the courts of a Member State within the EU jurisdictional zone.

West Tankers case confined to intra-EU litigation

The UK Supreme Court, in the AES case discussed above,32 confirmed that the ECJ’s decision in West Tankers does not preclude the use of anti-suit injunctions against parties contemplating bringing, or already actively pursuing, proceedings in the courts of a country which is not a Member State of the EU or of the Lugano Convention system.

The position following the EU Jurisdiction Regulation (2012)

The intra-EU prohibition on anti-suit injunctions, as imposed by West Tankers, has not been lifted. The recast Jurisdiction (or Brussels) Regulation (2012),33 however, makes clear that a judgment on the substance of a case is binding even though a decision by a Member State’s court involved a preliminary decision rejecting the suggestion that the matter was subject to a valid arbitration clause.
(2) Hong Kong

In *Lucky Sun Development Ltd v Gainsmate International Ltd* (2007), the plaintiff commenced arbitration proceedings in Hong Kong after the defendant started litigation in Mainland China. The plaintiff sought various orders from the Hong Kong court under s 2GC of the Arbitration Ordinance (Cap 341) which was then in force. This provision empowered the Court to make ancillary orders in support of arbitration proceedings. In a nutshell, the plaintiff sought mandatory injunctions in Hong Kong to restrain the Mainland proceedings and was successful in obtaining ex parte orders enjoining the defendant from continuing the Mainland proceedings pending the conclusion of the Hong Kong arbitration. The defendant then sought to discharge the ex parte orders on the ground of material non-disclosure, principally the plaintiff’s failure to inform the judge about the dispute over the tax liability involved and the principles of law governing anti-suit injunctions, together with other grounds, including lack of urgency. Deputy Judge Chan, who heard the defendant’s application, found that the injunction requested by the plaintiff was an anti-suit injunction and held that the plaintiff should have alerted the Deputy Judge to the principles governing such injunctions. Refusing the injunction sought, he held that there was “insufficient justification in this case to justify an interference with the Mainland Proceedings”.  

It would be interesting to see whether and to what extent an anti-suit injunction granted by a Hong Kong court in support of arbitration would be recognised or enforced by the Mainland courts. With regard to those Asian jurisdictions that follow English common law but have also adopted the UNCITRAL Model Law, it would also be interesting to see how and to what extent the English common law principles governing anti-suit injunctions interact with the court’s powers to grant such injunctions under art 17J of the Model Law (court-ordered interim measures). It should, however, be noted that, although the current Hong Kong Arbitration Ordinance (Cap 609) has adopted the 2006 version of the Model Law, s 45 of the Ordinance applies in substitution for art 17J.

Part III: Enforcement of a foreign award that has been annulled by a court of the seat, where that court lacked independence

(1) England

In the *Yukos* litigation, four Russian arbitral awards had been annulled by a Russian court. When the matter of enforcing the awards was considered by the Dutch courts, the Amsterdam Court of Appeal held that the Russian court which had purportedly annulled the award had in fact lacked judicial independence. The Amsterdam court proceeded to enforce the Russian awards. The principal sum (US$ 425 million) had been paid. Proceedings were brought in England to seek recovery of interest of US$ 160 million, being additional compensation attributable to dilatory satisfaction of the award by the award-debtor.

The English Court of Appeal in the *Yukos* case (2012) held that the questions whether the Russian court’s decision had been vitiated by extraneous pressure and whether that court lacked impartiality and independence had been resolved by the Amsterdam Court of Appeal, applying a Dutch test of public policy. This meant that the issue before the English court was not the same, because it required the English court to apply in this regard, independently and afresh, English public policy.

The English Court of Appeal’s approach in the *Yukos* case is attractive. It would be problematic, indeed unacceptable, if the English courts were in effect to abdicate responsibility for testing whether foreign courts lacked impartiality and
independence by instead deferring under the rubric of issue estoppel to a third country’s prior determination of this point.

Later in the Yukos litigation, Simon J held, in Yukos Capital Sarl v OJSC Rosneft Oil Co (2014) that (1) the English courts can award interest (under s 35A of the Senior Courts Act 1981) on a foreign arbitral award, (2) a foreign award could be recognised in this manner, even though it had been annulled by the courts of the foreign seat, provided that (3) the foreign Russian judicial annulment is itself invalid under English conflict of laws principles. With regard to point (3), Simon J held that the Russian judicial annulment proceedings would not be recognised, applying “conventional English conflict of law principles”, where, for example, the judgments annulling the awards were obtained by fraud, or it would be contrary to public policy to enforce them, or they were obtained in breach of the rules of natural justice.

(At the time of writing, Simon J’s decision is under appeal to the English Court of Appeal, though permission to appeal has been confined to relatively narrow points concerning the calculation of interest. It is understood that the central point decided by Simon J – that the Russian awards remain open to enforcement in England – is not the subject of appeal.)

It would be problematic, indeed unacceptable, if the English courts were in effect to abdicate responsibility for testing whether foreign courts lacked impartiality and independence by instead deferring under the rubric of issue estoppel to a third country’s prior determination of this point."

(2) Hong Kong

In Astro Nusantara International BV v PT Ayunda Prima Mitra (a Hong Kong Court of First Instance judgment dated 17 February 2015), Astro sought to enforce five SIAC arbitral awards in Hong Kong. Enforcement of the awards by the 6th-8th applicants in the arbitration (‘Additional Parties’) against First Media had been refused by the Singapore Court of Appeal by a judgment of that court rendered on 31 October 2013 (the ‘SCA Judgment’), on the ground that there was no valid arbitration agreement between the Additional Parties and First Media and that the arbitral tribunal had no jurisdiction to make the awards in favour of the Additional Parties against First Media.

Notwithstanding the SCA judgment, the Hong Kong Court of First Instance held that Astro would still be able to enforce a judgment in Hong Kong on the basis of these arbitral awards. This was because, on the facts, Anderson Chow J held that First Media should not be permitted to rely on s 44(2) of the previous Arbitration Ordinance (Cap 341) to resist enforcement of the awards because it had acted in breach of the principle of good faith. Further, the learned judge refused to exercise his discretion to extend the time for First Media to apply to set aside the Hong Kong orders granting leave to Astro to enforce the awards in Hong Kong and the Hong Kong judgment that gave effect to the awards pursuant to s 2GG of the previous Ordinance.
In particular, it was considered that although First Media had successfully resisted the enforcement of the awards before the Singapore Court of Appeal, the Singapore court was acting in its capacity as the enforcement court and not as supervisory court. The awards have not been set aside. They are still valid and create legally binding obligations on First Media to satisfy them.

Concluding remarks

In Part II of this article, the authors noted judicial support for arbitration agreements by the grant of anti-suit injunctions, notably in the AES case. In Part III, the authors noted the complex interplay in the Yukos litigation between foreign arbitral proceedings, foreign supervisory judicial proceedings and successive attempts to recognise the relevant foreign awards, despite the courts of the seat having purported to rescind those awards. The Astro case shows a pragmatic and pro-enforcement approach to the enforcement of foreign arbitral awards.

1 The authors are grateful to the members of the HKI Arb (under the Presidency of Samuel Wong) and to Squire, Patton, Boggs (Peter Chow) and the Council members of HKI Arb for their hospitality and interesting discussion.


3 According to Mustill & Boyd, Commercial Arbitration: 2001 Companion (2001, London: Butterworths), pp 23 et seq, there are four ‘pillars’ and not three. The learned authors refer, however, to four features of the Arbitration Act 1996 (ss 1, 33 and 40, together with s 4 and Sch 1); these aspects differ from the three pillars of agreement, autonomy, and international enforcement discussed in the present article.

4 “…[T]he court’s general approach should be a minimalist one of intervening only within the framework of the Act or in order to support the basic process of arbitration”: Hiscox Underwriting Ltd v Dickson Manchester & Co Ltd [2004] 1 All ER (Comm) 753, per Cooke J at [41].


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10 [2012] 1 Lloyd’s Rep 671, applied in Arsanovia Ltd v Cruz City 1 Mauritius Holdings [2013] 2 All ER (Comm) 1.

11 These include (other matters within Sch 1 are not mentioned here), the following provisions of the 1996 Act: ss 9-11 (stay of legal proceedings), 24 (power of court to remove arbitrator), 29 (immunity of arbitrator), 66 (enforcement of award), and 67 and 68 (challenging the award: substantive jurisdiction and serious irregularity).

12 1996 Act, ss 33, 40(1); Mustill & Boyd, op cit (note 3 above), pp 30-37. Editorial note: see also s 1(a) of the 1996 Act.

13 As noted in Ceteme SA v Roust Holdings Ltd [2005] 1 WLR 3555, 3571, at [61], per Clarke LJ. Editorial note: see also s 1(c) of the 1996 Act.

14 Ibid, at [61]. See also AES Ust-Kamenogorsk Hydropower Plant LLP v Ust-Kamenogorsk Hydropower Plant JSC [2012] 1 WLR 920 at [96], [97] and [107], per Rix LJ. [203]-[205], per Stanley Burnton LJ.


16 Fiona Trust and Holding Corporation v Privolav, also known as Premium Natta Products Ltd v Fil Shipping Co Ltd [2008] 1 Lloyd’s Rep 254 (HL). See discussion per Lord Hoffmann at [17]-[19].


19 Lesotho Highlands Development Authority v Impreglio Spa [2006] 1 AC 22.

20 Bandwith Shipping Holdings v Intaari [2006] EWHC 2532 (Comm), at [77]; Arduina Holdings BV v Celtic Resources plc [2006] EWHC 3155 (Comm) at [45].

21 1996 Act, s 46(1).

22 Ibid, ss 45(1), 69.

23 Report on the Arbitration Act 1996 (November 2006), at [66]-[69]. Editorial note: The report was prepared jointly by (principally) the Commercial Court Users’ Committee, the British Maritime Law Association and the London Shipping Law Centre.


25 [2003] 1 WLR 1041 (PC), at [14] and [15], per Lord Hobhouse.


27 Gouvernement du Pakistan v Société Dallah Real Estate & Tourism Holding Co (Cour d’appel de Paris, 17 February 2011).

28 [2013] 1 WLR 1889.

29 Leading commentators have noted the dichotomy of an arbitration agreement’s positive and negative obligations and effects: eg, G Born, International Commercial Arbitration (2nd Edn, 2014), notably at 1253 et seq.


32 [2013] 1 WLR 1889.

33 European Parliament and Council Regulation (EU) No 1215/2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast), which took effect on 10 January 2015. As to its non-application to arbitration, see Preamble, para (12). Editorial note: In Gazprom OAO v Republic of Lithuania, Case C-536/13 (13 May 2015), the Grand Chamber of the Court of Justice of the EU (CJEU) gave a preliminary ruling under art 267 of the Treaty on the Functioning of the European Union (TFEU) on the question whether (inter alia) the enforcement of an arbitral award rendered by an arbitral tribunal seated in an EU Member State, containing orders enjoining a party from bringing claims in the courts of an EU member state, contravened the Regulation’s predecessor, Council Regulation (EU) No 44/2001 on jurisdiction and the recognition of judgments in civil and commercial matters. The CJEU clarified that awards of arbitral tribunals and their recognition and enforcement fall outside the scope of the Brussels Regulation as tribunals are not State courts (at [36]). Distinguishing West Tankers, it held that (1) the Regulation “must be interpreted as not precluding a court of a Member State from recognising and enforcing, or refusing to recognise and enforce, an arbitral award prohibiting a party from bringing certain claims before a court of that Member State” (at [44]); and (2) the recognition and enforcement of awards containing anti-suit injunctions is therefore exclusively a matter governed by the procedural law of the Member State and the New York Convention (at [42]).

34 [2007] HKEC 2045.

35 Editorial note: For a recent case in which the Court of First Instance granted an anti-suit injunction under s 45(2) of the Arbitration Ordinance (Cap 609) to restrain the pursuit of litigation in Turkey in favour of arbitration in Hong Kong, see Ever Judger Holding Co Ltd v Kroman Celik Sanayii Anonim Sirketi, [2015] 3 HKC 246.


37 [2013] 1 All ER 223.


39 Ibid. See [12] and [15]-[22] for an illuminating discussion.


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The Use of Emergency Arbitration Provisions

Michael Dunmore

This article examines the implementation and use of emergency arbitration, particularly in Asia, by reference to comparison of the rules of leading arbitral institutions. It also gives an overview of how emergency arbitration has developed over the short period in which it has been in existence.

Introduction

Emergency arbitration is a feature of the rules of all leading international arbitration institutions, both across Asia and elsewhere. Emergency arbitration is considerably new and likely to remain a permanent part of the international arbitration landscape.

Prior to the modern day emergency arbitration provisions, precursor emergency arbitration rules existed, such as the International Chamber of Commerce (ICC) Pre-Arbitral Referee procedure, as well as optional emergency arbitrator provisions in the rules of the American Arbitration Association. The emergency arbitration rules implemented in the Stockholm Chamber of Commerce (SCC) Rules (2010 Edn) may, however, be said to be the first instance of the modern form of emergency arbitration rules. Since these rules were promulgated, other leading arbitration institutions have followed suit, issuing comparable rules with a variety of refinements.

“... [M]any legal counsel are not aware of the high threshold that has been put in place in order for an arbitrator to have jurisdiction over an emergency arbitration. This is likely due in part to the fact that most rules do not outline this high threshold clearly.”
Filing an emergency arbitration claim

One notable aspect of emergency arbitration is the comparison of fees for filing a request for emergency arbitration as between the various institutions.

In filing a request for emergency arbitration under the Singapore International Arbitration Centre (SIAC) Rules, the cost consists of a filing fee of S$ 5000 and a minimum of S$ 20,000 for the arbitrator’s fee (totaling US$ 18,000). Under the Kuala Lumpur Regional Centre for Arbitration (KLRCA) Rules, the cost is a US$ 2,000 filing fee and an arbitrator’s fee of US$ 10,000. Under the Japan Commercial Arbitration Association (JCAA) Rules, an administration fee of ¥216,000 is charged for filing an application for emergency arbitration, as well as a deposit of ¥100,000 that will go towards the arbitrator’s fee of ¥2,160,000 (total cost US$ 19,900). Under the ICC Rules the cost is US$ 40,000.

The Hong Kong International Arbitration Centre (HKIAC) emergency arbitrator fees are based on the hourly rate of an arbitrator and administrative expenses. When filing a request for emergency arbitration under the HKIAC Administered Arbitration Rules, (HKIAC Rules), the claimant must pay an application deposit that will cover administration expenses and arbitrator’s fees. Under the China International Economic and Trade Arbitration Commission (CIETAC) Rules, emergency arbitrator fees are based on an hourly fee. Under the International Centre for Dispute Resolution (ICDR) Rules, there is no filing fee; parties must, however, pay the emergency arbitrator an hourly fee, plus the arbitrator’s expenses. An article summarising the first eight ICDR emergency arbitration cases indicates that emergency arbitrators spent between 10 and 40 hours in each emergency arbitration. From this estimate of time spent in the ICDR cases, using an hourly rate has the potential for considerable cost savings when compared with the flat fee approach.

Once a request for emergency arbitration is filed, it must be accepted by the relevant arbitration institution. In determining whether to accept a request, the institution conducts a very general prima facie review of it before appointing an emergency arbitrator, in order to ensure that all requirements for filing the request have been satisfied. After this initial review has been conducted and an emergency arbitrator has been appointed, the emergency arbitrator will, at the outset of the proceedings, apply a strict test of whether there is a prima facie case on the merits and whether the claimant has demonstrated both urgency and that, without relief, it would suffer irreparable harm. This is a difficult threshold to meet, in particular in satisfying the issues of urgency and irreparable harm. A report published by the SCC indicates that in five of the nine cases received by the SCC between 2010 and 2013, the arbitrators found that this threshold had not been met. The ICC appears to have had similar experiences, with emergency arbitrators having rendered emergency orders in only four out of the 10 applications for emergency arbitration received.

Frequency of the use of emergency arbitration provisions

In terms of actual use, a number of arbitral institutions have recently published reports on the use of their emergency arbitration provisions. The SIAC has provided an overview of its experiences with the 34 applications received during the period 2010-2014, with that number increasing to 42 at the end of 2014. The ICDR reported 28 emergency arbitrations. The SCC provided a summary of each of the nine cases it received between 2010 and 2013, with that number increasing to a total of 13 in 2014. Similarly, the ICC published a report outlining the 10 emergency arbitration cases filed under the emergency arbitrator provisions included in the ICC Rules of Arbitration (2012 Edn). It has additionally been reported that the Kigali International Arbitration Centre received one emergency arbitration within its first two years of operation. These reports vary in detail, with those of the SCC and ICC being the most comprehensive.

One striking difference between the SIAC emergency arbitration provisions and those of other arbitration centres is that the SIAC Rules provide for the retrospective application
of its emergency arbitration provisions to agreements entered into before those provisions were implemented. This may explain why the SIAC has received so many applications for emergency arbitration. By contrast, other rules, such as those of the HKIAC and ICC, provide for emergency arbitration if the arbitration agreement relied on was entered into after the emergency arbitration provisions were included in those rules; emergency arbitration has, therefore, not yet been available in many arbitrations.

"Despite Hong Kong and Singapore including relevant provisions to facilitate the enforcement of emergency arbitration orders, not all jurisdictions are so enforcement-friendly—in particular, China, where only courts may grant interim relief."

Enforceability and implementation

Despite the questionable enforceability of emergency arbitration awards under the New York Convention, there exists case law in the US that demonstrates a willingness by the courts to uphold an order by an emergency arbitrator on grounds of equitable relief to support arbitration pending the outcome of a final award. Another US court has upheld an emergency arbitration award where the respondent unsuccessfully argued that the emergency arbitrator acted outside of his authority. Both of these cases illustrate that the decision of an emergency arbitrator is likely to be upheld by the courts; each of these cases involved challenges at the seat. To this author’s knowledge, there are no decisions in which the enforcement of an emergency arbitration award has been sought in a jurisdiction other than the seat.

With regard to arbitration rules providing for emergency arbitration, one noteworthy aspect of the ICC Rules, by contrast with those of various other institutions, is that the former provide that the decision rendered by an arbitral tribunal is termed an ‘order’ and not an ‘award’. Making this distinction avoids the issue of whether what is decided by an emergency arbitrator can be considered as an award. This is particularly prudent because such a determination is not final and binding and, as a result is unlikely to be enforceable under the New York Convention. Similarly, the SCC Rules use the phrase “emergency decision on interim measures”. It is noteworthy to mention that the HKIAC Rules provide that an interim measure may be in the form of an order or an award. In this regard, at least in the US, courts would not be constrained by formalistic distinctions of the label applied to a tribunal’s decision, whether an order or an award. Furthermore, a preliminary order to protect assets is final under the US Federal Arbitration Act.

A number of jurisdictions, such as Hong Kong, have amended their international arbitration legislation to provide explicitly for the enforcement of “any emergency relief granted, whether in or outside Hong Kong, by an emergency arbitrator.” This provision avoids any potential problems of the classification of a decision. Furthermore, by taking this particularly welcome step, Hong Kong has made clear that it will enforce emergency arbitration awards rendered outside of the territory. To similar effect, the definition of ‘arbitral tribunal’ in Singapore’s International Arbitration Act (Cap 143A) has been amended to include an emergency arbitrator. Strangely, however, the Singapore Act has not adopted arts 17H and 17I of the UNCITRAL Model Law (2006 version), which have been adopted by other Model Law jurisdictions, such as Hong Kong (albeit in a slightly modified form). These articles are particularly important, in that they aid the enforceability of emergency arbitration decisions: art 17H provides for enforcement, while art 17I provides grounds for denial of enforcement.

Despite Hong Kong and Singapore including relevant provisions to facilitate the enforcement of emergency
arbitration orders, not all jurisdictions are so enforcement-friendly – in particular, China, where only courts may grant interim relief. The most recent CIETAC Rules reflect this: they include provisions on interim relief that have been drafted to refer parties arbitrating in Mainland China to a court for conservatory measures. Where parties arbitrate outside of Mainland China, emergency arbitrator rules comparable to those of other leading centres are available for interim relief. In China, mandatory laws prohibit an arbitral tribunal from issuing interim measures, which would also likely apply to emergency arbitration awards.

As such, it is doubtful whether an emergency arbitration decision would be enforceable in China. This is despite Hong Kong and Mainland China having entered in 1999 into an agreement regarding the mutual enforcement of awards, as this agreement governs only the enforcement of awards and does not pertain to orders. Furthermore the agreement permits a court in Mainland China to refuse enforcement of an award if enforcement would be contrary to the public interest of Mainland China. This agreement is necessary for the enforcement of Hong Kong awards in Mainland China, as Hong Kong is a Special Administrative Region (SAR) of China, so that the New York Convention does not apply to the enforcement of Hong Kong awards in Mainland China (and vice versa). Hong Kong and Macao (which is also an SAR) entered into a similar agreement in 2014, permitting the mutual enforcement of awards made in each jurisdiction. The agreement of 1999 was reflected in the previous version of the Hong Kong Arbitration Ordinance (Cap 341), while that of 2014 is reflected in amendments made in 2014 to the current Arbitration Ordinance (Cap 609).

From a combination of case law and legislative ingenuity across jurisdictions, it appears that there are tools in place that provide for the enforcement of emergency arbitration awards. This is with the exception of China, which provides a counterbalance in the form of uncertainty as to whether emergency arbitration awards are enforceable under the New York Convention.

"From a combination of case law and legislative ingenuity across jurisdictions, it appears that there are tools in place that provide for the enforcement of emergency arbitration awards. This is with the exception of China ...

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Conclusion

The reporting of emergency arbitration decisions is particularly useful in a number of respects. Such reporting provides practitioners with an understanding of how frequently emergency arbitration has been utilised, as well as how often claimants have been successful in obtaining emergency relief. From this author’s experience working in the secretariat of an arbitration institution, many legal counsel are not aware of the high threshold that has been put in place in order for an arbitrator to have jurisdiction over an emergency arbitration. This is likely due in part to the fact that most rules do not outline this high threshold clearly. The HKIAC Rules are an example of institutional rules that do provide parties with a clear picture of the required threshold, which is particularly helpful for parties considering whether to commence an emergency arbitration.

Perhaps the most controversial aspect of emergency arbitration awards is their enforceability. It is most likely the case that emergency arbitration awards fall short of being considered as a final award under the New York Convention. Based on the cases discussed above as well as legislative ingenuity, however, it appears that emergency arbitration awards will be upheld by a court in most instances. The best approach to take in clarifying this uncertainty is to amend legislation, as Hong Kong and Singapore have done, in order to ensure the enforceability of such awards.

1. An emergency arbitrator’s fees are capped at 20% of those of a sole arbitrator.
8. Lundstedt, op cit (note 3 above) at pp 3-25.
10. Carlevaris & Feris op cit (note 4 above). Prior to the implementation of the emergency arbitrator provisions, the ICC dealt with 14 pre-arbital referee decisions.
12. An award must be final under the New York Convention.
17. Hong Kong Arbitration Ordinance (Cap 609), s 22B.
19. Article 23 and Appendix III (effective 1 January 2015).
22. Article 23.4: “When deciding a party’s request for an interim measure under Article 23.2, the arbitral tribunal shall take into account the circumstances of the case. Relevant factors may include, but are not limited to: (a) harm not adequately reparable by an award of damages is likely to result if the measure is not ordered, and such harm substantially outweighs the harm that is likely to result to the party against whom the measure is directed if the measure is granted; and (b) there is a reasonable possibility that the requesting party will succeed on the merits of the claim. The determination on this possibility shall not affect the discretion of the arbitral tribunal in making any subsequent determination.”
ADR in Asia
27 October 2015
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SAVE THE DATE

30 years of resolving disputes
The CIETAC Arbitration Rules 2015

Yeung Man Sing

This article introduces and comments upon the major changes made by the 2015 Edition of the CIETAC Arbitration Rules. It also introduces and explains CIETAC’s Guidelines on Evidence (2015 Edn).

Introduction


The previous edition of CIETAC’s Arbitration Rules (the 2012 Rules) had taken effect on 1 May 2012. Soon afterwards, an internal jurisdictional dispute broke out between CIETAC Beijing and its two sub-commissions in Shanghai and Shenzhen, which resulted in the two sub-commissions declaring independence, renaming themselves and introducing their own sets of arbitration rules.\(^1\)

To cope with the jurisdictional uncertainty created by this situation, reforms to CIETAC’s administrative structure were required. The introduction of the 2015 Rules was seen as a timely attempt to address the aftermath of the situation.

In tandem with the 2015 Rules, CIETAC has also published Guidelines on Evidence (the Guidelines). These were adopted on 26 September 2014 and took effect on 1 March 2015.

The 2015 Rules are perhaps the most important edition to have been issued in recent years. Taken together with the Guidelines, they are intended to bring CIETAC arbitration more into line with best international arbitration practice.

The 2015 Rules are discussed below. The status of individual provisions, whether new or revised, is indicated in the section headings.
Reconstituted structure and an Arbitration Court (new provisions)

CIETAC has established a new Arbitration Court, which performs functions under the 2015 Rules under the joint direction of the authorised Vice Chairman of CIETAC and the President of the Arbitration Court.²

The Arbitration Court performs the administrative functions of its predecessor, the CIETAC Secretariat. In addition, it is given case management powers over some newly introduced procedures, such as those relating to joinder of parties, consolidation of multiple arbitrations and emergency arbitration, all of which are discussed below.

“The 2015 Rules are perhaps the most important edition to have been issued in recent years. Taken together with the Guidelines [on Evidence], they are intended to bring CIETAC arbitration more into line with best international arbitration practice.”

The 2015 Rules are perhaps the most important edition to have been issued in recent years. Taken together with the Guidelines [on Evidence], they are intended to bring CIETAC arbitration more into line with best international arbitration practice.

Service of documents by public notary recognised (new provisions)

Service of documents by public notary is now more readily recognised. Any arbitration correspondence addressed to a party or its representative(s) shall be deemed to have been properly served on that party if, provided that all other ordinary means of service have failed, it is sent to that party by other means that can provide a record of the attempt at delivery, including but not limited to service by public notary, entrustment or retention.⁴

Single arbitration for multiple contracts (new provisions)

A party may now initiate a single arbitration proceeding with regard to disputes arising out of or in connection with multiple contracts, provided that there is sufficient proximity, that is, where –

terminated, or (iii) the parties’ agreement is ambiguous as to the designated sub-commission/arbitration centre.³ This provision is aimed at eliminating uncertainties stemming from the CIETAC internal dispute and its aftermath. Despite this, however, it should be noted that the provision is not binding on the courts in China. The actual scope and effect of this provision would therefore depend upon the willingness of a court to honour it when the court is seised of a relevant case.

The structure of CIETAC, including its sub-commissions and arbitration centres, is now set out clearly in Appendix I to the 2015 Rules. This provides a good reference point for drafters of arbitration agreements, so that they may draft their arbitration clauses in precise accordance with the respective names of the sub-commissions/arbitration centres.

In relation to any application for arbitration purportedly submitted to a CIETAC sub-commission/arbitration centre, the Arbitration Court is empowered to accept the application where (i) the sub-commission/arbitration centre agreed upon by the parties does not exist, or (ii) the agreed sub-commission/arbitration centre’s authorisation has been
“(a) such contracts consist of a principal contract and its ancillary contract(s), or such contracts involve the same parties as well as legal relationships of the same nature; (b) the disputes arise out of the same transaction or the same series of transactions; and (c) the arbitration agreements in such contracts are identical or compatible.”

**Joinder of additional parties (new provisions)**

A party to an arbitration may file a Request for Joinder in order to apply to join an additional party to the arbitration if the requesting party can establish that the arbitration agreement invoked in the arbitration *prima facie* binds the additional party. Where the application is filed after the formation of the arbitral tribunal, a decision shall be made by CIETAC after the arbitral tribunal hears from all parties, including the additional party, if the tribunal considers the joinder necessary. CIETAC has the power to decide not to join an additional party where the latter is *prima facie* not bound by the arbitration agreement invoked in the arbitration, or where any other circumstance exists that makes the joinder inappropriate.

The additional party is given as fair an opportunity of nominating the arbitral tribunal as the original parties. If the tribunal has already been formed, the additional party may still request the opportunity to nominate an arbitrator, and the original parties will have to nominate their desired arbitrators again.

**Consolidation of arbitrations (revised provisions)**

Procedures for the consolidation of arbitrations were first introduced by CIETAC under the 2012 Rules. CIETAC could consolidate several arbitrations at the request of a party or on its own initiative, so long as all parties agreed to consolidation.

Under the 2015 Rules, by contrast, CIETAC may consider consolidation only at the request of a party, but not on its own initiative. Consolidation may be ordered where –

“(a) all of the claims in the arbitrations are made under the same arbitration agreement; (b) the claims in the arbitrations are made under multiple arbitration agreements that are identical or compatible and the arbitrations involve the same parties as well as legal relationships of the same nature; (c) the claims in the arbitrations are made under multiple arbitration agreements that are identical or compatible and the multiple contracts involved consist of a principle [sic] contract and its ancillary contract(s); or (d) all the parties to the arbitrations have agreed to consolidation.”

Consent of all parties is no longer a prerequisite to consolidation but merely one of the grounds on which CIETAC may rely in making a decision whether to order consolidation. This represents a fundamental change to CIETAC’s approach, in that it now has power to order compulsory consolidation against the wishes of a party, by contrast with its previous approach of giving full party autonomy.

Nevertheless, in deciding whether to consolidate an arbitration, CIETAC is expressly required to take into account the opinions of all parties and other relevant factors, such as the correlation between the arbitrations concerned, including the nomination and appointment of arbitrators in the separate arbitrations. In the premises, CIETAC will be required to give a good reason if it decides to order consolidation in the face of objection by one party.
Interim relief (revised provisions)
Since the adoption of the 2012 Rules, parties have been able to request interim measures from the arbitral tribunal during the arbitration. The tribunal could order or award any interim measure it considered necessary or proper in accordance with the applicable law, and require the requesting party to provide appropriate security for costs in connection with any such measure. Under the 2015 Rules, the tribunal may also order or award any interim measure it deems necessary or proper in accordance with the agreement of the parties.

Emergency relief (new provisions)
The 2015 Rules also provide a mechanism whereby a party may request emergency relief pursuant to Emergency Arbitrator Procedures (the Procedures), under which an emergency arbitrator may make an emergency order or award that is binding upon both parties.

Appendix III of the 2015 Rules sets out the provisions of the Procedures. When submitting an application for emergency relief, the applicant shall attach the relevant documentary and other evidence on which the application is based, including but not limited to the arbitration agreement and any other agreements giving rise to the underlying dispute. After a preliminary review on the basis of the application, the arbitration agreement and relevant evidence submitted by the applicant, the Arbitration Court will decide whether the Procedures apply and, if so, the President shall appoint an emergency arbitrator.

To ensure the expeditious grant of relief, an express timetable is specified by the Procedures. The President shall appoint an emergency arbitrator within one day upon receipt of a request for emergency relief and payment of an advance of costs by the requesting party. The emergency arbitrator shall establish a procedural timetable for the proceedings, preferably within two days from acceptance of his/her appointment. The decision of the emergency arbitrator (which shall take the form of an order and not an award) shall be made within 15 days from acceptance of the appointment.

Despite the absence of relevant wording in the Rules, however, it would appear that the Procedures apply only to arbitrations administered by the CIETAC Hong Kong Arbitration Center, as such procedures are not readily available in Mainland China. A party seeking emergency relief in Mainland China must therefore apply to a court for appropriate measures under the current legal regime in that jurisdiction.

An order for emergency relief granted by an emergency arbitrator appointed under the Procedures, whether in or outside Hong Kong, is enforceable in Hong Kong in the same manner as an order or direction of the court (if leave to enforce is granted by the Hong Kong court). The decision of the court as to whether such leave should be granted is not subject to leave to appeal.

Conduct of the hearing (revised provisions)
As under the 2012 Rules, and unless otherwise agreed by the parties, the arbitral tribunal has a discretion to examine the case in any way it deems appropriate, provided that it acts impartially and fairly, and affords a reasonable opportunity to both parties to present their cases.

Under the 2015 Rules, a wide discretion is reserved to the presiding arbitrator, who, with the authorisation of the other
members of the tribunal, may decide upon the procedural arrangements for the arbitral proceedings at his/her own discretion.\textsuperscript{23} This discretion is subject to the presiding arbitrator’s duty to act impartially and fairly.

**Summary Procedure (revised provisions)**

Chapter IV of the 2015 Rules (arts 56-64) now govern the Summary Procedure. The monetary threshold for the mandatory application of the Summary Procedure is raised from an amount in dispute not exceeding RMB 2,000,000 to an amount not exceeding RMB 5,000,000. Even if the amount in dispute exceeds the threshold, parties may still adopt the Summary Procedure if one party applies for it and the other agrees, or if both parties agree to apply for it.\textsuperscript{24}

**Special provisions for CIETAC arbitration in Hong Kong (new provisions)**

Following the resumption of sovereignty by China in 1997, Hong Kong has maintained its independent common law system, pursuant to its status as a Special Administrative Region of China in accordance with the Basic Law. Because Hong Kong is a separate legal jurisdiction, its arbitration law (the Arbitration Ordinance (Cap 609 of the Laws of Hong Kong)) is fundamentally different from that of China (the Arbitration Law of 1994). Therefore, arbitration rules that are applicable in China may not be compatible with the law of Hong Kong.

CIETAC Hong Kong Arbitration Center (CIETAC-HKAC) was established in September 2012. To facilitate arbitrations administered by CIETAC-HKAC in Hong Kong, special provision is made in the 2015 Rules.\textsuperscript{25}

Unless otherwise agreed by the parties, the place of arbitration for an arbitration administered by CIETAC-HKAC shall be Hong Kong, the arbitration law applicable to the arbitral proceedings shall be that of Hong Kong, and the arbitral award shall be a Hong Kong award,\textsuperscript{26} which shall be affixed with the seal of CIETAC-HKAC.\textsuperscript{27}

Parties to CIETAC-HKAC administrations are expressly allowed, even without the consent of the other party, to nominate arbitrators from outside the CIETAC Panel of Arbitrators, subject to confirmation by the Chairman of CIETAC.\textsuperscript{28} This practice differs from arbitrations administered by other CIETAC sub-commissions/arbitration centres, whereby one party may nominate outside arbitrators only with the consent of the other party.

CIETAC-HKAC adopts a fee schedule\textsuperscript{29} separate from that which applies to arbitrations held at other CIETAC sub-commissions/arbitration centres. It is also noteworthy that CIETAC-HKAC may exercise a lien over the arbitral award to secure payment of outstanding fees of the arbitrators and all expenses due.\textsuperscript{30}

**Arbitrators’ special remuneration (new provisions)**

CIETAC has inherent power to charge parties, apart from the standard fees set out in fee schedules I and II to Appendix II, for other additional and reasonable actual costs, including but not limited to arbitrators’ special remuneration. Under the 2015 Rules, the Arbitration Court will determine the chargeable special remuneration, after hearing from the arbitrator and the party concerned, with reference to the scales of arbitrators’ fees and expenses set out in Arbitration Fee Schedule III to Appendix II,\textsuperscript{31} ie, the fee schedule applicable to CIETAC-HKAC arbitrations.

“… [T]he special provisions of the 2015 Rules relating to CIETAC-HKAC arbitration mark an important milestone for CIETAC, as they signify its expansion into Hong Kong, China’s gateway to the world and the world’s window into China.”
The CIETAC Guidelines on Evidence

For many years, there has been uncertainty as to whether and, if so, to what extent, the rules of evidence used in civil litigation in China are applicable to arbitrations. The only relevant provision in China’s Arbitration Law is that the parties shall produce evidence in support of their claims and that the tribunal may collect evidence on its own if it considers this necessary. In practice, tribunals have broad discretion to determine the admissibility of evidence and would usually admit evidence in accordance with China’s Civil Procedure Law.

In order to assist the parties, their counsel and arbitral tribunals in dealing with issues of evidence more efficiently in arbitration proceedings, CIETAC adopted the Guidelines in accordance with China’s Arbitration Law, the 2015 Rules and CIETAC arbitration practice, and with appropriate reference both to the IBA Rules on the Taking of Evidence in International Arbitration (2010 Edn) (IBA Rules) and Chinese principles of evidence in civil litigation that are suitable for use in arbitration. By having tailor-made the Guidelines rather than simply adopting the IBA Rules, CIETAC aims to introduce a set of evidence rules that are more compatible with China’s unique legal system. The salient provisions of the Guidelines are highlighted below.

**Burden of proof**

Articles 1-3 of the Guidelines illustrate the burden of proof suggested in arbitration proceedings. It is worth noting that the claimant would have the burden of proving its case even if the respondent were to default in the arbitration proceedings without good cause.

**Submission, taking and exchange of evidence**

Articles 4-14 of the Guidelines suggest procedures for the submission, taking and exchange of evidence in arbitration proceedings. In relation to the production of evidence, the
Guidelines provide procedures for general as well as specific discovery. The arbitral tribunal also has power to request a party to produce evidence or collect evidence itself during arbitration proceedings, in either case on its own initiative.\textsuperscript{34}

Examination of evidence

Articles 15-17 of the Guidelines suggest procedures for the examination of evidence in arbitration proceedings. For arbitrations conducted by way of oral hearing, all documentary evidence submitted shall be exhibited and be subject to oral examination by the parties at the hearing. All witnesses and expert witnesses shall in principle be subject to direct examination and cross-examination, either by appearing in person at the hearing or by way of a videoconference.\textsuperscript{35}

Assessment of evidence

Articles 18-24 of the Guidelines suggest procedures for the assessment of evidence in arbitration proceedings. In general, the tribunal has sole discretion to determine the admissibility, relevance, materiality and weight of evidence.\textsuperscript{36}

In similar fashion to the IBA Rules, the Guidelines are not intended to be mandatory rules in arbitration proceedings. They do not form an integral part of the 2015 Rules and their application is subject to the consent of the parties in each case. The parties may agree to adopt the Guidelines as a whole, or in part, or in part but with variations, or to use them for guidance or reference only, without binding effect.

Summary and conclusion

CIETAC’s overall efforts at reform in recent years are well recognised by the arbitration community. The 2015 Rules continue the long-standing process of bringing CIETAC arbitration practice into line with best international standards and practice.

In particular, the special provisions of the 2015 Rules relating to CIETAC-HKAC arbitration mark an important milestone for CIETAC, as they signify its expansion into Hong Kong, China’s gateway to the world and the world’s window into China. Together with the evidence rules set out in the Guidelines, which are highly compatible with arbitral practice in China, the 2015 Rules make CIETAC an increasingly appealing option for both Chinese and foreign parties seeking to arbitrate.\textsuperscript{37}

Editorial note: for discussion and practical advice to users, see Clarisse von Wunschheim & Lear Liu, The CIETAC Feud – Why it’s a Mess and How to Avoid being Caught in the Middle (2013) Asian DR 78.

1 Article 2(2) of the 2015 Rules.
2 Ibid, art 2(6).
3 Ibid, art 8(3).
5 Ibid, art 18(1).
6 Ibid, art 18(7).
7 Ibid, art 18(5).
8 Ibid, art 19(1), other grounds being sufficient proximity in the arbitrations.
9 Ibid, art 19(2).
10 Ibid, art 23(3).
11 Ibid, art 23(2).
12 Ibid, Appendix III, art 1(3).
13 Ibid, Appendix III, art 2(1).
14 Ibid, Appendix III, art 2(1).
15 Ibid, Appendix III, art 5(1).
17 Ibid, Appendix III, art 6(1).
19 Ibid, Appendix III, art 6(2).
20 Arbitration Ordinance (Cap 609), s 22B(1).
21 Ibid, s 22B(4).
22 2015 Rules, art 35(1).
23 Ibid, art 35(5).
24 Ibid, art 56(1).
26 Ibid, art 74.
27 Ibid, art 78.
28 Ibid, art 76.
29 Ibid, Appendix II, CIETAC Arbitration Fee Schedule III.
31 2015 Rules, art B2(1).
33 Guidelines, art 3.
34 Ibid, art 11.
36 Ibid, art 18.
Will the Winds of Change on Internal Appellate Proceedings in Arbitration Reach Asia? – Part 2

Mauro Rubino-Sammartano & Dr Shahla Ali

This article discusses the tensions between the desire for swift and final decisions in arbitration and the desire of parties to seek redress for erroneous decisions. A result of this is the increasing adoption by international arbitral institutions of internal mechanisms of appellate review. Part 1, which was published in the April 2015 issue, introduced the internal review process of the European Court of Arbitration and discussed the contrasting lack of such processes under Asian commercial arbitration rules. This Part discusses internal review processes under the rules of a number of other international arbitral institutions.

**Annulment of investment awards under the ICSID Convention**

The commercial arbitration community is largely not in favour of internal avenues of appeal against arbitral awards. It is, however, well known that the Washington (ICSID) Convention 1965 provides for a two-stage review of investor-State awards. Article 52 of that convention provides in this regard that “either party may request annulment of the award …”, even if only on procedural grounds. If the award is challenged, its validity is considered by an *ad hoc* Committee of three members appointed by the Chairman of the ICSID Centre.

The principle of review by an appellate arbitral tribunal rather than by State courts has therefore been accepted by ICSID and such applications are not infrequent. This is in contrast with the position under the Arbitration Rules of the European Court of Arbitration (1997 Edn) (the ECA Rules), under which the requirement for appellants to deposit the amount due under the original award tends to act as a deterrent to applications for review by that institution.¹
It is, however, submitted that a limit on the efficacy of ICSID’s internal appellate mechanism lies in the fact that the authority of an ad hoc Committee is limited to annulling the original award. The Convention provides:

“If the award is annulled the dispute shall, at the request of either party, be submitted to a new Tribunal, constituted in accordance with Section 2 of this Chapter.”

It is therefore necessary for the losing party who succeeds on internal review to submit the dispute to a new arbitral tribunal. In the Klockner and Amco Asia cases, the award made by the first arbitral tribunal had been annulled, and the decision by the second tribunal had been the object of a further application for its annulment. The four degrees of these proceedings are reported to have lasted for, respectively, nine and ten years, which is not exactly what was expected by the parties, who believed they were entitled to a quick and favourable decision.

The AAA Optional Appellate Arbitration Rules
Being aware of dissatisfaction among several well-informed users, some leading arbitral institutions have introduced internal appeal processes into their rules.

The American Arbitration Association (AAA) issued revised Optional Appellate Arbitration Rules (the AAA Optional Appellate Rules) in 2013. A quick comparison between these Rules and the ECA Rules is made below.

As their title suggests and their provisions state, the AAA Optional Appellate Rules are optional. Consequently, if the parties wish to exercise this option, they must expressly provide for it in writing. This approach differs from that under the ECA Rules, which provide that the parties are entitled to apply for review by an appellate arbitral tribunal, unless they opt out in writing.

The second difference between the two sets of rules is that, while the ECA Rules provide for a de novo “full review of the dispute, by way of rehearing, including in particular as to admissibility, the facts and the merits”, the AAA Optional Appellate Rules provide for a standard of review which – even if greater than that allowed by existing federal and state statutes – is stricter than the ECA’s standard, since the AAA standard is limited to –

“(1) an error of law that is material and prejudicial; or (2) determinations of facts that are clearly erroneous”.

The requirement that an error on a point of law be “material and prejudicial” and that the determination of a fact be “clearly erroneous” inevitably limits the grounds for such an appeal. The appellate arbitral tribunal’s decision is significantly limited by the provision that “the appeal tribunal may not order a new arbitration hearing or send the case back to the original arbitrator(s) for correction or further review”.

Such a limit on review under the AAA Optional Rules to a clearly erroneous determination of fact does not include errors as to admissibility of evidence – which is a discretionary issue – nor the relevance of evidence and other issues pertaining to the merits.

The principle of review by an appellate arbitral tribunal rather than by State courts has … been accepted by ICSID and such applications are not infrequent.

From a user-friendliness perspective, one positive feature of the AAA Optional Rules is the requirement that the appeal be made simply by filing a Notice of Appeal. This leaves to a subsequent stage the full pleading of the statement of facts and of the arguments.

A further provision of the AAA Optional Rules deals with the effects of the appeal. This states that as an award pending...
internal appellate review (the 'Underlying Award') “shall not be considered final for purposes of any court actions to modify, enforce or vacate the Underlying Award (judicial enforcement proceedings), … the time period for commencement of judicial enforcement proceedings shall be tolled during the pendency of the appeal.” It provides further that “the parties agree to stay any already initiated judicial enforcement proceedings until the conclusion of the arbitral appellate process.”

In some jurisdictions, however, the effect of the appeal may need to be provided for by statute, the agreement of the parties not being sufficient to achieve the desired result. The AAA Optional Rules rightly remind parties that, even if they opt for an appeal, their right to apply to State courts for amendment of the award (such as correction or a complementary decision on an issue which has not been covered by the award) is not excluded.

The AAA Optional Rules follow normal US practice whereby the arbitral institution offers the parties a list of members of its panel and invites them to select arbitrators jointly from that list. In one sense, this is an alternative to the approach under the ECA Rules, whereby a preliminary meeting may be convened with the parties by the ECA Secretariat for the purpose of allowing them to nominate the three arbitrators jointly. The two sets of rules diverge with regard to oral argument. Parties may present oral argument as of right under the ECA Rules, whereas this is discretionary under the AAA Optional Rules, which provide that “(a) unless otherwise directed by the appeal tribunal, all appeals will be determined upon the written documents submitted by the parties”.

In line with other arbitration rules, the AAA Optional Rules confer immunity on both the arbitral institution and arbitrators. No such provision is made by the ECA Rules.

The AAA Optional Rules further provide for the possibility that the losing party shall be ordered to pay the reasonable costs and fees of the proceedings, while the ECA Rules provide that costs shall follow the event.

In the authors’ opinion, the AAA Optional Rules are very well drafted and the AAA is to be congratulated on them.

The CPR Arbitration Appeal Procedure

The International Institute for Conflict Prevention and Resolution (CPR) has drawn renewed attention to its Arbitration Appeal Procedure (the CPR Procedure) by referring to it in its General Commentary on its recent CPR Administered Arbitration Rules (2013 Edn). In that commentary, the CPR acknowledges that, on the one hand, “most users of arbitration find the finality of an arbitral award appealing” while, on the other, some parties to major cases “are concerned about the possibility of an aberrant award and would like to be able to appeal from such an award to a tribunal of outstanding appellate arbitrators”.

This statement therefore represents the CPR’s perception of winds of change in the aspirations of well-informed users of arbitration who have experienced the negative impacts of the lack of an internal arbitral appeal mechanism and who no longer share the former general sense of antipathy towards such a mechanism.

Like the AAA Optional Rules, the CPR Procedure is also optional to users. The option may be exercised by providing for it in writing, either in the arbitration clause in their underlying contract or in a post-dispute arbitration agreement.

The CPR Procedure is drafted so as to apply to arbitrations conducted in the United States, whether pursuant to the CPR Non-Administered Arbitration Rules (2007 Edn) or otherwise.
Like the AAA Optional Rules, the CPR Procedure deals with the effect of an appeal, such that “the Original Award shall not be considered final for purposes of seeking judicial confirmation enforcement, vacatur or modifications”, this status being reserved to the appellate award.

The CPR Procedure further provides that an appeal amounts to an irrevocable waiver of “the right to initiate court action to seek to confirm, enforce, vacate or modify the Original Award until the appeal process has been completed”, and that “any statutory time period for the commencement of court actions to confirm, enforce, vacate or modify arbitral awards shall be tolled …”

The grounds for appeal that must be shown are (i) “material and prejudicial errors of law of such a nature that … [the Original Award] does not rest upon an appropriate legal basis”, or (ii) that the Original Award is based upon “factual findings clearly unsupported by the record”, or (iii) that there exist “one or more of the grounds set forth in Section 10 of the Federal Arbitration Act [FAA] for vacating an award”, ie, for matters such as arbitrator corruption, fraud, evident partiality, misconduct and excess of powers. Where FAA-based objections are raised, appellate tribunals have no power to remand the original award.

The parties and the appellate arbitral tribunal are enjoined to “use their best efforts to avoid delay and to assure [sic] that the Appeal will be concluded within six months of its commencement.”

In line with this case management target, appellate proceedings are to be commenced by a written notice of appeal. The other party may serve a written cross-appeal. The appellant is allowed one opening brief and one response brief. Ordinarily, the other party (the appellee) is allowed one response brief; if, however, the appellee is also a cross-appellant, it shall be allowed a second brief.

A party is entitled to submit oral arguments, if it so requests or the tribunal deems it necessary.

An appellate arbitral tribunal under the CPR Procedure comprises three arbitrators, unless the parties agree in writing to a sole arbitrator. The parties are invited to select them jointly from a list of candidates listed on the CPR’s Appellate Panel.

The liability of the CPR and/or of any member of the arbitral tribunal for any act or omission is excluded, “except for willful [sic] misconduct”.

Judicial review of arbitral awards by State courts

By contrast with the certainties that internal appellate review mechanisms are capable of encouraging, the review of arbitral awards by national courts can, on the one hand, give rise to uncertainty as to the scope of review or, on the other, demonstrate limitations in it.

In Renusagar Power Co Ltd v General Electric Co, the Supreme Court of India held that an award may be set aside if it is contrary to the public policy of India, or to the interests of India, or to justice or morality. This did not include setting aside of the award based on an error of law or fact.

The scope for challenging an award on the merits was later widened by the Supreme Court of India’s decision in Oil...
and Natural Gas Corporation Ltd v Saw Pipes Ltd,\(^3\) where the additional ground of ‘patent illegality’ was included as a ground for annulling an award. The Court said:

“… But in a case where the judgment and decree is challenged before the Appellate Court or the Court exercising revisional jurisdiction, the jurisdiction of such Court would be wider.

“Therefore, in a case where the validity of [the] award is challenged there is no necessity of giving [sic] a narrower meaning to the term ‘public policy of India’. On the contrary, wider meaning is required to be given so that the ‘patently illegal award’ passed [sic] by the arbitral tribunal could be set aside … Similarly, if the award is patently against the statutory provisions of substantive law which is in force in India or is passed [sic] without giving an opportunity of hearing to the parties as provided under Section 24 [of India’s Arbitration and Conciliation Act 1996] or without giving any reason [sic] in a case where parties have not agreed that no reasons are to be recorded, it would be against the statutory provisions. In all such cases, the award is required to be set aside on the ground of ‘patent illegality’.” (Per Shah J)

Furthermore, the Supreme Court held in Venture Global Engineering v Satyam Computer Services Ltd\(^4\) that a challenge to a foreign award in India would also have to meet a challenge related to the merits that the award is “patently illegal”.\(^4\)

As such, it should be considered that, in India, one must satisfy not only the grounds required under art V of the New York Convention in challenging the enforcement of a foreign award, but also the public policy grounds under s 34 of the Indian Arbitration and Conciliation Act 1996 in challenging an award at the seat.

This view is also to be found in relation to challenges to Chinese arbitral awards. Under art 58 of China’s Arbitration Law of 1994, courts in China have the power to review the merits of a domestic award in deciding whether to set it aside. Article 58(5) permits a court to consider whether evidence has been withheld. Article 58 also permits a court to set aside an award which it considers contrary to the public interest.

It should, however, be noted that awards issued in China but which concern a foreign element, known as ‘foreign-related’ awards, may only be set aside in China on certain procedural grounds. Under art 70 of the Arbitration Law, ‘foreign-related’ awards may only be set aside if they involve any of the circumstances listed in art 260(1) of China’s Civil Procedure Law of 1991 (now art 258 of the revised Civil Procedure Law of 2008). By contrast with the position in domestic arbitration, this provision does not permit withheld evidence or the public interest to be be considered as grounds for setting aside ‘foreign-related’ awards. Furthermore, under the pre-reporting system of the Supreme People’s court (SPC), a lower People’s Court may not set aside a foreign-related award unless its decision is ultimately confirmed by the SPC, pursuant to the latter’s Notice on Certain Issues concerning the Setting Aside of Foreign-related Arbitral Awards by the People’s Court issued on 23 April 1998.

This view as to the challenge of awards on the merits is not to be found elsewhere in South East Asia. In Government of the Republic of the Philippines v Philippine International Air Terminals Co Inc,\(^5\) the High Court of Singapore held (per Judith Prakash J at para 38):

“… [A]n arbitral award is not liable to be struck down on application in the courts because of allegations that it was premised on incorrect grounds whether of fact or of law. An application to set aside an award made in an international arbitration is not an appeal on the merits and cannot be considered in the same way as the court would consider the findings of a body over whom it had appellate jurisdiction.”

Similarly, The Tokyo District Court took a ‘taboo’ view as to appeals on the merits in KK Descente v Adidas-Salomon AG,\(^6\) where it adopted the views of the New Zealand Court of Appeal in Methanex Motunui Ltd v Spellman.\(^7\) In the latter decision, the
Court of Appeal held, pursuant to art 34 of Schedule 1 to New Zealand’s Arbitration Act 1996 (which corresponds broadly to art 34 of the UNCITRAL Model Law), that –

“Article 34 is expressed in exclusionary terms: it specifies the only grounds upon which a Court may interfere with an award in review proceedings. Accordingly, it is not open to the parties to a submission to arbitration to confer, by contract, a more extensive jurisdiction on the Court, for instance to review for factual error. On this (perhaps literal) approach, a contractual stipulation which further limits the grounds upon which review is available merely supplements Article 34 and does not derogate from it.” (Per McGrath, William Young and O’Regan JJ at [105])

Conclusion
The wish of the party having a proper claim to obtain a fast decision from arbitration is to be respected. If, however, an award has been made wrongly, it is suggested that such party would prefer the error to be redressed instead of having to live with a faster but erroneous result. By contrast with arbitration, parties to litigation have a well-established right to a de novo review.

As discussed previously, parties refer disputes to arbitration in the expectation of having not only a dispute resolution process that differs from State court proceedings, but also a better process – otherwise, they would continue to use litigation. If, however, arbitration does not grant to the losing party the right to a full de novo review, it is suggested that the arbitral process is worse, not better, than litigation.

Among the various arguments used by the many opponents of internal arbitral review mechanisms, a main one is that reaching the ‘final’ arbitral decision would take much more time. If, however, the first instance proceedings last one year, it is quite possible that the appellate proceedings could last no more than 6 months. The ‘final product’ (ie, the appellate award) would then be available within 18 months, which, it is submitted, is quite an acceptable duration for a fully reviewed award, even when compared to the duration of commercial arbitration proceedings, which frequently (though not always) last for two years and sometimes much longer. Through the medium of published debate between a senior law professor and arbitrator, Pierre Mayer, and a leading construction law scholar, Ian Duncan Wallace, Professor Mayer stated in clear terms that, if State courts could review the merits of an arbitral award, arbitration would become only a prelude to court proceedings. He did, however, add that he saw no objection to an appellate arbitral tribunal reviewing the merits of the original award. Several years after the ECA’s introduction of an internal arbitral appeal mechanism, leading international arbitrators Howard Holtzmann and Stephen Schwebel wrote in support of appellate arbitral review.

It is therefore submitted that internal arbitral appeal mechanisms do not weaken the structure and attractiveness of arbitration, but strengthen it.

“… [I]nternal arbitral appeal mechanisms do not weaken the structure and attractiveness of arbitration, but strengthen it.”
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The Far Reaching Consequences of Expert Evidence

John Molloy

This article briefly reviews the history of expert evidence in common law courts and discusses the sources and content of the fundamental duties of the party-appointed expert, illustrated by reference to cases in which experts have failed to comply with these duties. It is the edited text of the 9th Annual Winnie Whittaker Memorial Lecture, which was delivered by the author at HKIAC on 14 May 2014.

Introduction

The earliest known use of an expert witness in English law that I am aware of was in *Folkes v Chadd* (1782). This English case concerned a harbour in Norfolk that had silted up. The Court accepted evidence from a leading civil engineer, John Smeaton. In his judgment, Lord Mansfield CJ said:

“It is objected that Mr Smeaton is going to speak, not to facts, but as to opinion. That opinion, however, is deduced from the facts which are not disputed; the situation of the banks, the course of the tides and winds and the shifting of the sands. His opinion, deduced from all these factors is that, mathematically speaking, the bank may contribute to the mischief, but not sensibly. Mr Smeaton understands the construction of harbours, the causes of their destruction and how remedied. … I have myself received the opinion of Mr Smeaton respecting mills, as a matter of science. The cause of the decay of the harbour is a matter of science, and still more so, whether the removal of the bank can be beneficial. Of this, such men as Mr Smeaton alone can judge. Therefore we are of the opinion that his judgment, formed on facts, was proper evidence.”

The Court’s decision to accept evidence from an expert witness is widely cited as the root of modern rules on expert evidence. There have, however, been more recent cases that have also formed the basis of the modern rules on expert evidence, two of which I mention below.
In the *Ikarian Reefer case* (1993), Cresswell J set out the duties of an expert witness in a format that has been used in many notes, guidelines and protocols. Two particular duties to which I wish to draw attention concern independence.

1. Expert evidence presented to the court should be, and should be seen to be, the independent product of the expert, uninfluenced as to form or content by the exigencies of litigation.
2. An expert witness should provide independent assistance to the court by way of objective unbiased opinion in relation to matters within his expertise.

In the Australian case of *R v Bonython* (1984), the Court posed two questions that needed to be addressed before expert evidence would be allowed.

1. Whether the subject matter of the opinion falls within the class of subjects upon which expert testimony is permissible. This question sub-divided into two parts:
   - (i) whether the subject matter is such that a person without instruction or experience in the area of human experience would be able to form sound judgment on the matter without the assistance of witnesses in possession of special knowledge or experience in the area; and
   - (ii) whether the subject matter of the opinion forms part of the body of knowledge or experience which is sufficiently organised or recognised to be accepted as a reliable body of knowledge or experience, a special acquaintance with which by the witness would render his opinion of assistance to the court.
2. Whether the witness has acquired by study or experience sufficient knowledge of the subject to render his opinion of value in resolving the issue before the Court.

Three fundamental attributes of expert witnesses arise from these cases: Knowledge – Independence – Honesty.

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Three fundamental attributes of expert witnesses arise from … [the decided] cases: Knowledge – Independence – Honesty.

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The process of giving expert evidence

The giving of expert evidence is a process whereby a person gives an opinion on technical matters to assist a court or arbitral tribunal in determining liability and/or entitlement, on the basis of the factual evidence to be found and held by the court or tribunal.

An expert should follow the process independently of any potential outcome, and of the behaviour and demands both of parties to a dispute and of others involved in the matter.

For the expert, providing evidence is not about winning or losing but about providing a knowledgeable, independent and honest opinion, and then explaining that opinion through expert reports and oral evidence.

Straightforward, one would hope, but today it is painfully and sadly obvious that opinion evidence is often provided in the absence of one or all of the fundamental attributes.

There exists a general mistrust of experts

Just over 60 years after John Smeaton gave evidence, the role of the expert witness had already become troublesome. Judge John Pitt Taylor, in his *Treatise on the Law of Evidence* (first published in 1848), described several classes of expert witnesses whose testimony should be viewed with caution and concluded that –

“… perhaps the testimony which least deserves credit with a jury is that of skilled witnesses. ... It is often quite surprising to see with what facility and to what extent their views can be made to correspond with the wishes and interests of the parties who call them.”
There were other similar comments around that time, as found in the judgments in *Lord Abinger v Ashton* (1873)⁶ and *Thorn v Worthing Skating Rink Co* (1877)⁷ – and the mistrust is still with us today.

In March 2012, the British Channel Four News programme broadcast an investigation, *How competent are expert witnesses?*, with particular reference to experts in the fields of psychology and family court matters. It found that 20% of experts in such fields were not sufficiently qualified.⁸ In May 2012, a report in ‘The Times’ of London highlighted the poor quality of experts, apparent lack of impartiality, lack of qualifications, and the giving of evidence outside their area of expertise.⁹

**The problems**

It is important that experts should not accept an appointment if they are not going to be left to form their own opinion without fetter and interference. If experts consider that their opinion in a case has been constrained in any way, then they are duty bound to make that known to the court or tribunal.

In many areas of expertise, there can be reasonably divided opinion and, in this situation, it would be obvious for a client to choose an opinion that is closest to its own position: but, that is quite different to an expert tailoring an opinion to meet the client’s required outcome.

The fee arrangement is often another area of concern. It is my view that an expert should never be engaged on a lump sum basis and absolutely never on a contingency arrangement.

A lump sum fee potentially restricts an expert’s ability to assist the Court or tribunal fully because, subconsciously or otherwise, an expert is in danger of curtailing work in line with a lump sum fee, while a contingency fee is clearly inconsistent with the duty of independence. Most, if not all, professional guidelines and protocols state that an expert should be paid at hourly rates on the basis of the time reasonably spent.

The way to avoid constraints is for the process to ensure that experts are required to work in accordance with rules and regulations set down by many regulatory bodies.

In this regard, it is my view that arbitral tribunals, in particular, should order and direct that certain protocols and regulations be followed. Further, they should order that experts include within their opinion reports not only their instructions but also details of their fee arrangements. Unfortunately, this happens far too infrequently.

**Selection of the expert**

In a paper on expert evidence by Professor Samuel R Gross of the University of Michigan Law School,¹⁰ a lawyer is quoted as having said:

“Usually I like my expert to be around 50 years old, have some grey in his hair, wear a tweedy jacket and smoke a pipe. You must recognise that jurors have prejudices and you must try to anticipate these prejudices. … Some people may be geniuses but because they lack training in speech and theater they have great difficulty in conveying their message to a jury.”¹¹

An expert should be chosen with thorough and careful consideration. One must be aware that, despite the above quote, it does not necessarily follow that age, qualifications, years in the industry, standing in a particular industry or previous appointments make for a good expert. If an expert is knowledgeable, independent and honest, those attributes will carry through in their evidence, from the opinion reports to the giving of oral evidence.
The required attributes for an expert therefore come with integrity and ability – not age, qualifications, experience, standing and previous appointments.

Look at factual witnesses who often have no experience in giving evidence and being in the witness box. Those who are honest come across well – they can explain themselves fully as they have nothing to hide. Granted, they may not be as polished and eloquent as an advocate but, unlike an advocate, there are no clever acts of persuasion or intimidation that a witness, whether factual or expert, should be performing.

In any event, the purpose of giving evidence is to clarify and test an opinion and, although advocates can turn this part of the process into a spectacle, and often do, they do so merely for the benefit of their client. I say this because, in my experience, a court or tribunal takes little interest in such theatrics.

So how does the Court decide whether an expert is sufficiently knowledgeable? In *R v Bunniss* (1964), a Canadian case, the Court commented that the manner in which a skill or expertise had been acquired was immaterial, the focal point being whether that skill was possessed by the expert:

“The test for expertness so far as the law of evidence is concerned is skill and skill alone in the field of which is sought to have the witness’s opinion. I adopt, as a working definition of the term ‘skilled person’, one who has by dint of training and practice, acquired a good knowledge of the science or art concerning which his opinion is sought. It is not necessary, for a person to give opinion evidence of a question of human physiology, that he be a doctor of medicine.”

It is clear from this that the knowledge of an expert is viewed not by reference to academia but by ability.

There are an amazing number of cases in which the Courts have found that experts either lacked the knowledge or strayed outside their area of expertise to give opinion on matters that they should not. Illustrative cases include *SPE International Ltd v Professional Preparation Contractors (UK) Ltd* (2002), in which the expert was found not to have specialised knowledge in the area in which he was giving expert evidence, and the infamous Oscar Pistorius murder trial in South Africa (2014), in which Roger Dixon, an expert witness for the defendant Paralympic athlete, was accused of irresponsibly giving evidence.

“An expert should follow the process independently of any potential outcome, and of the behaviour and demands both of parties to a dispute and of others involved in the matter.”

In *London Underground Ltd v Kenchington Ford Plc* (1999), HH Judge Wilcox was unimpressed by the expert evidence produced on behalf of London Underground Ltd (LUL). It was clear that LUL’s engineering expert had not taken into account all the parameters for design that had faced Kenchington. Worse, that expert appeared more concerned to assume the role of advocate of his client’s case rather than to demonstrate fairness, objectivity and a proper awareness of the role of the expert witness. Ultimately LUL’s expert evidence was condemned as being invalid and unscientific. No doubt the expert would, on paper, have been perceived as being a good expert.

In *Carla Homes South Ltd v Sir Alfred McAlpine Homes East Ltd* (1995), an expert witness called Francis Goodall was an architect with considerable experience of acting as an expert. He had in fact had over 120 appointments in such a capacity, and was additionally a member of the Committee of the Society of Construction Arbitrators. All in all, he was a man who should have needed no reminders as to his role as expert witness and would have been perceived as being a good expert.
In 1990, however, Mr Goodall had written a paper entitled *The Expert Witness: Partisan with a Conscience*. In this extraordinary article he had said:

“How should the expert avoid becoming partisan in a process which makes no pretence of determining the truth but seeks only to weigh the persuasive effects of arguments deployed by one adversary or the other. … If an expert witness is able to so present the data that they seem to suggest an interpretation favourable to the side instructing him, that is, it seems to me, within the rules of our particular game, even if it means playing down or omitting some material consideration.”

\[\text{For the expert, providing evidence is not about winning or losing but about providing a knowledgeable, independent and honest opinion, and then explaining that opinion through expert reports and oral evidence.}\]

The Court took a very dim view of these comments, which it clearly thought completely discredited Mr Goodall’s evidence. Laddie J commented:

“The whole basis of Mr Goodall’s approach to drafting of an expert’s report is wrong. The function of a court of law is to discover the truth relating to the issues before it. In doing that it has to assess the evidence adduced by the parties. The judge is not a rustic who has chosen to play a game of Three Card Trick. He is not fair game. Nor is the truth. That some witnesses of fact, driven by a desire to achieve a particular outcome to the litigation, feel it necessary to sacrifice truth in pursuit of victory is a fact of life. The court tries to discover when it happens. But in the case of expert witnesses the court is likely to lower its guard. Of course the court will be aware that a party is likely to choose as its expert someone whose view is most sympathetic to its position. Subject to that caveat, the court is likely to assume that the expert witness is more interested in being honest and right than in ensuring that one side or another wins. An expert should not consider that it is his job to stand shoulder to shoulder through thick and thin with the side which is paying his bill. ‘Pragmatic flexibility’, as used by Mr Goodall, is a euphemism for ‘misleading selectivity’.”

In *Clonard Developments Ltd v Humberts (a firm)* (1999), the trial judge (whose decision was upheld by the Court of Appeal) rejected the evidence of both of the parties’ expert valuers in the following terms:

“In my judgment, the evidence of both these witnesses was unhampered by impartiality. As is all too often the case, each adopted the role of advocate for the case which he was called to support and in the result, save where their evidence relates to factual matters, I am unable to accord very much weight to the opinions expressed.”

In *London Fire and Emergency Planning Authority (LFEPA) v Halcrow Gilbert Associates Ltd* (2007), the dispute concerned an allegation of professional negligence arising from a fire which occurred in a building specifically designed to train fire fighters on how to put out fires. Unfortunately, the fire in question was not one lit for training purposes but a real fire that was not meant to have happened. LFEPA maintained that the fire was a result of Halcrow’s alleged negligence and relied extensively upon four experts. In respect of three of these experts, HH Judge Toulmin was severely critical, saying that the evidence of one was “… partial, biased, and on occasions misleading to such an extent that it could not be described as independent”, observing that another reached a “conclusion that was wholly unsustainable” and stating that a third gave rise to concern as to his “lack of independence as an expert”.

**Conclusion**

The process of giving expert evidence is unfortunately still...
flawed after so many years and despite attempts to regulate it. But why does this happen? The truth is that the role and responsibilities of an expert often do not align with the objectives of a client and/or its lawyers. This can manifest itself in a number of ways:

(1) a lack of understanding of the process;
(2) sticking to a timetable that narrows down the choice of expert due to availability;
(3) seeking a specific fee arrangement that should be unacceptable to a good expert;
(4) a weak position, and therefore seeking an expert to advocate that position at a minimal cost.

Further, an expert is too quick to abandon his/her role and responsibilities to a court or arbitral tribunal, or is simply unaware of the process of giving expert evidence.

It would be disappointing if further restraints had to be put in place – for example, if there were a more noticeable move towards regulating appointed experts, because this would seem to represent a failure of a legal system and of the concept that a party is free to present its case in the manner it wishes.

If, however, matters are not improved upon, then we are left with the situation envisaged by Professor Gross in his paper on expert evidence, in which he says:

“One of the most unfortunate consequences of our system of obtaining experts is that it breeds contempt all round. The contempt of lawyers and judges for experts is famous. They regularly describes expert witnesses as prostitutes, people who live by selling services that should not be for sale. … No other category of witness, not even parties, is subject to such vilification. This attitude is not compatible with the serious attention to evidence that these presumably untrustworthy witnesses provide. On the other side, some of the best experts in many fields have a contempt for legal proceedings that goes beyond a low regard for law and lawyers that is common in our society. They believe, correctly, that experts who agree to testify are subject to strong pressures to become partisan of the side that calls them. They also feel (again correctly) that not only is the process of providing evidence difficult and time consuming, but that they are treated in a demeaning manner and that their evidence is poorly used. As a result, these experts refuse to be witnesses, leaving the field to those with fewer scruples or fewer options.”

For those of us who are involved in expert witness work, the quotation above makes depressing reading. The consequences of experts who are not knowledgeable, independent or honest are indeed far reaching. They demean the role of the expert and undermine any legal process.

My advice to a client or lawyer is therefore to choose an expert that a court or arbitral tribunal would wish to have before it, ie, one who would give the same opinion free of any constraints and irrespective of the appointing party.

1 (1782) 3 Doug KB 157, (1782) 99 ER 589.
2 (1782) 3 Doug 157 at 159, (1782) 99 ER 589 at 590.
4 Editorial note: The so-called ‘Cresswell principles’ were largely a summation of principles laid down in previous cases.
5 (1848) 18 SASR 44 at 46-47, per King CJ (Supreme Court of South Australia).
6 (1873) 17 LR Eq 368.
7 (1877) 6 Ch D 415.
11 Ibid, at p 1133.
12 R v Bunniss (1964) 50 WWR (NS) 422 at 424, per HH Judge Tyrwhitt-Drake (British Columbia County Court).
16 (1990) 56 Arbitration (JCIArb) 159-161.
20 Ibid, at [64].
21 Ibid, at [76].
22 Ibid, at [81].
23 Op cit (note 10 above), at pp 1135-1136.
A Welcome Decision of the Hong Kong Courts on the Seat of the Arbitration

Sheila Ahuja & Chantal du Toit

Introduction
In a positive move by the Hong Kong Court of First Instance, Mimmie Chan J has upheld an agreement to arbitrate where ambiguity arose in the context of the arbitration clause. The decision in Z v A demonstrates the continuing trend of the Hong Kong courts adopting a pro-arbitration approach, reaffirming the territory’s position as a key player on the international arbitration stage.

Factual background
The Agreements
Party Z (the Applicant) and Party A (the 1st Respondent) entered into two separate agreements for the manufacture, sale and purchase of goods in Mainland China: a CKD and Agency Agreement dated 20 April 2007 (the ‘CKD Agreement’) and a Technical Cooperation Agreement dated 2 June 2007 (the ‘TC Agreement’). Both agreements provided for arbitration as a means of dispute resolution in the following terms.

CKD Agreement
“In case of breach of any of the Articles of this agreement by either of the parties, both Parties agree to put best efforts to remedy by negotiations [sic]. Otherwise, those Parties agree to arbitration as per the International Chamber of Commerce and held in CHINA? ... [sic]” (Emphasis added)

TC Agreement
“Any dispute, controversy or difference which may arise between the parties out of or in relation to this Agreement or for the breach thereof shall be settled amicably by the parties, but in case of failure, it shall be finally settled in CHINA by arbitration pursuant to the Rules of the International Chamber of Commerce whose award shall bind the parties hereto.” (Emphasis added)
The CKD Agreement provided that it was to be governed by the laws of the People’s Republic of China (PRC). The TC Agreement was silent on the governing law of the underlying contract, though it was accepted by both parties that the applicable law was that of the PRC.

A dispute arose between the parties. The Respondents (the 1st Respondent and companies affiliated with it) commenced ICC arbitration proceedings. Whilst the proceedings were brought pursuant to the arbitration clause contained in the CKD Agreement, relief was sought in respect of the Applicant’s alleged breach of both of the Agreements.

The ICC Court thereafter appointed a sole arbitrator in the proceedings (the Tribunal). One of the issues framed for determination was whether the Tribunal had jurisdiction to deal with the issues in dispute.

The Tribunal’s decision

A hearing duly took place on the matter. The Tribunal rendered a partial arbitral award in which it acknowledged that the ICC Court had fixed the place of arbitration as “Hong Kong, PR China”. On this basis, the Tribunal determined that the procedural law to be applied to the arbitration, including as to determination of the Tribunal’s jurisdiction, was Hong Kong law.

The Applicant then brought a jurisdictional challenge before the Hong Kong Court of First Instance under s 34 of the Hong Kong Arbitration Ordinance (Cap 609) (the Ordinance), which applies art 16 of the UNCITRAL Model Law, seeking a declaration that the Tribunal had no jurisdiction in the matter and that the partial award should therefore be set aside.

The Hong Kong Court’s decision

The Court declined to set aside the award. Instead, Mimmie Chan J endorsed the findings of the ICC Court and the Tribunal and held that the arbitration should be conducted in Hong Kong. The Court ultimately found that the Tribunal had been properly constituted and that it had jurisdiction over the dispute in question. Costs were awarded against the Applicant on an indemnity basis.

The Court’s analysis on the seat of the arbitration

The key question before the Court was whether or not the decision that Hong Kong was the place of arbitration was correct by reference to the parties’ agreement to arbitrate. The issue was really whether the reference to “China” in the agreement to arbitrate meant Mainland China or Hong Kong.

The place, or ‘seat’, of an arbitration, has wide-ranging implications for parties. It determines the procedural law applicable to the arbitration. More importantly, the courts of the seat will have exclusive supervisory jurisdiction over the arbitration proceedings and awards, for example, with respect...
to the setting aside of an award. In her judgment, Mimmie Chan J explained the importance of the law of the seat and its potential interplay with various other different legal systems in the context of an international arbitration.\(^2\)

In endorsing the decisions of the ICC Court and the Tribunal that the seat of the present arbitration was Hong Kong, the Court undertook a stage-by-stage analysis.

**Correctness of the decision as to the Tribunal’s jurisdiction**

The starting point of the analysis was that the role of the Court in a jurisdictional challenge under s 34 of the Ordinance was to decide the correctness of the ruling by the Tribunal on its own jurisdiction (citing *Dallah Real Estate and Tourism Holding Co v Ministry of Religious Affairs of the Government of Pakistan*\(^4\)). Notwithstanding this *de novo* review, however, it was made clear that the Court plays a limited and narrow role, which should not encompass any inquiry into the merits of the dispute. Hence Mimmie Chan J decided that it was “necessary and important”\(^4\) that the present challenge be confined to the sole question of the Tribunal’s jurisdiction.

**Principles of contractual interpretation**

As this was ultimately a question as to the meaning of the parties’ agreement, the Court restated and endorsed the principles of contractual interpretation which were applicable in determining this issue.

The Hong Kong Court relied heavily on the landmark English case of *Fiona Trust & Holding Corporation v Privalov*,\(^5\) in which the House of Lords decided (in the context of interpreting an arbitration clause) that the judge should put himself in the position of rational businessmen when determining the intention of the parties at the time of entering into the contract. It also relied on findings of the courts (for example, Lord Hoffman’s observations in *Bank of Credit and Commerce International SA v Ali*\(^6\)) that parties are unlikely to have intended to agree to do something unlawful or legally ineffective and that the courts would therefore lean in favour of and prefer a construction which renders the contract enforceable and legal.

> “The … [‘seat’ of an arbitration] has wide-ranging implications for parties. It determines the procedural law applicable to the arbitration. More importantly, the courts of the seat will have exclusive supervisory jurisdiction over the arbitration proceedings and awards …”

**Construction of the reference to ‘China’**

In applying the principles stated above to the facts, the starting point of this part of the Court’s analysis was that, although parties are free to choose the precise manner of resolving their disputes, and the manner and content of their agreement to arbitrate, they should then be bound by that choice and the courts would hold them to their agreement.\(^7\)

In the present case, the parties, having agreed to the ICC Rules in their agreements to arbitrate, must be deemed to have agreed to abide by the rules and procedures of that body, and that this agreement was clear and could not be disputed.\(^5\)

The Court held that as reasonable, rational businessmen, the parties must have been aware at the time of entering into the Agreements that the PRC had resumed sovereignty over Hong Kong and that, legally as well as geographically, Hong Kong was a part of the PRC.\(^9\) The Court therefore decided that the parties, having provided that disputes be submitted to arbitration in “China”, could not be said to have agreed upon the place of arbitration, and that it would be artificial to hold that they had intended the arbitration clause to mean either “China excluding Hong Kong” or “China including Hong Kong”. That necessarily meant that the ICC Court was entitled and indeed bound to determine the place of arbitration under the ICC Rules, as this had not been specified by the parties. It could not, in the Court’s view, be incorrect for the ICC Court
to decide, “on a plain reading of the arbitration clauses”, that the arbitration should be held in Hong Kong, which is geographically and legally a part of China.  

In reaching its holding as to Hong Kong being the place of arbitration, the Court also considered the risks associated with the enforceability of an arbitral award rendered in Mainland China. In particular, the Court recognised that there was a risk that (1) an ICC award made in Mainland China might not be enforceable in Mainland China, and (2) ICC arbitration proceedings seated in Mainland China might not be subject to supervision by the Mainland courts under the PRC Civil Procedure Law of 2008 or the Arbitration Law of 1994. By contrast, the Court recognised that an ICC award made in arbitration proceedings conducted in Hong Kong would be enforceable in both Hong Kong and Mainland China, as well as other Contracting States to the New York Convention.  

Acknowledging that the objective of arbitration was to resolve disputes by rendering a final, binding and enforceable award, the Court held that the seat of arbitration should therefore be Hong Kong.

Commentary
A number of interesting observations may be made with respect to this judgment.

Willingness of the Hong Kong Court to uphold agreements to arbitrate
Z v A continues the trend of sophisticated arbitral jurisdictions upholding agreements to arbitrate on the logical and settled principle that parties will have intended agreements to arbitrate to be enforceable.

In particular, what is evident from the judgment is the Court’s willingness to construe the arbitration agreement in question in such manner as to give it the most effective interpretation. One of the principal reasons for deciding that Hong Kong should be the seat, for example, was to avoid any risk of Mainland courts refusing supervision of the arbitral proceedings or the arbitral award and any risk of the award being held to be unenforceable.

Interplay between the Hong Kong and Mainland China legal regimes
One of the most useful aspects of the judgment is its insightful observations about the interplay between the legal regimes in Hong Kong and Mainland China.

Hong Kong is generally viewed by the international community as an autonomous legal system, despite being a part of the PRC. Hong Kong’s autonomous status is crucial to the reputation of its courts, its investment landscape and, most importantly, its development as an international arbitration hub.

As observed in the judgment, when it comes to arbitration, Hong Kong and Mainland China have separate and distinct legal regimes, arbitral proceedings in each territory are supervised by different courts, and arbitral awards rendered in each territory are likewise enforced by different courts. At times, this can give rise to certain tensions, such as in the context of the dispute that arose in the present case from the vagueness of the language adopted by the parties. The territorial distinction is, however, generally clear, for example, in the context of international treaty-making. Whilst Hong Kong automatically acceded to certain treaties entered into by the PRC at the time of the resumption of sovereignty in 1997, it has continued to retain a degree of independence in relation to other international agreements. Most notably for the present purposes, Hong Kong, whilst having a sub-statual status, is recognised in its own right under the New York Convention, which provides for the enforcement of arbitral awards rendered in Hong Kong in 156 countries around the world, and vice versa.

The risks of arbitrating in China
Another aspect of the light shed by the Z v A case stems from the fact that one of the main considerations taken into account by the Court was the risks associated with arbitrating in Mainland China. Historically speaking, a key concern for international investors in Mainland China has been whether foreign arbitral institutions (such as the ICC) can administer arbitration proceedings seated in the PRC and whether arbitral
awards rendered by such institutions will be recognised as enforceable by the Mainland courts.

“One of the principal reasons for deciding that Hong Kong should be the seat, for example, was to avoid any risk of Mainland courts refusing supervision of the arbitral proceedings or the arbitral award and any risk of the award being held to be unenforceable.”

It is fair to say that Mainland China is slowly but surely taking steps to overcome the obstacles traditionally encountered by investors. The most significant development of late has been the landmark decision in Anhui Longlide Packaging and Printing Co Ltd v BP Agnati SRL, a case relied upon in the present judgment, in which the Supreme People’s Court held that an arbitration clause providing for ICC arbitration in Mainland China was in fact valid.

Despite this encouraging move, however, parties are still advised to be mindful of the risks of arbitrating in Mainland China. Broader concerns remain about the restrictive legislative framework in place: for example, the ICC continues to fall outside of the list of recognised arbitration institutions under the Arbitration Law of the PRC. There is also no system of judicial precedent in Mainland China (being a civil law jurisdiction), so that the Longlide decision will not have binding effect on other Mainland courts.

Conclusion
Z v A is a robust decision, to say the least. Some commentators may argue that the Court construed the reference to “China” too widely, on the basis that the parties would have referred to ‘Hong Kong’ had this been their intention. There is also an interesting question concerning the choice of court to hear the case. If the dispute had been referred to the Mainland courts, would they have upheld the ICC Court’s finding of a Hong Kong seat and would the ultimate outcome have been the same?

Nonetheless, what comes out of the judgment is a strong indication that the Hong Kong courts will uphold agreements to arbitrate to the fullest extent possible, in accordance with well-established principles of contractual interpretation.

On a practical level, the judgment serves as a welcome reminder to lawyers and corporations alike about the importance of drafting arbitration clauses in precise and unequivocal terms. As a drafting tip, parties choosing the seat of the arbitration are advised to specify a particular city within a country, rather than just the country, so as to avoid any confusion as to the place of arbitration. This is not simply a China-specific issue but, rather, one that extends to all countries having more than one major city or arbitration hub.
Construction Arbitration in Hong Kong: A Practical Guide

Reviewed by Neil Kaplan CBE QC SBS

Hong Kong’s emergence as one of the world’s leading financial and legal centres has spawned, over the past few decades, a busy construction arbitration industry. As Sir Vivian Ramsey points out in his preface to *Construction arbitration in Hong Kong: A practical guide*, the Construction Industry Council forecasts that –

“public and private sector construction work will rise from current levels of some HK$190 billion to HK$240 billion in the next ten years. Inevitably, this will give rise to disputes.”

Indeed, one rarely finds disputes lawyers in Hong Kong who have not worked on a construction case, particularly in arbitration.

For example, the construction of Hong Kong’s Chek Lap Kok airport itself generated a number of high profile disputes, while the operation of the airport – and its air traffic control system in particular – continues to titillate the minds of Hong Kong’s construction lawyers. The need for sophisticated construction dispute expertise prompted the creation of Hong Kong’s Construction and Arbitration List in the 1980s. It is thus no surprise that Hong Kong’s construction dispute environment has grown to be remarkably refined when it comes to the complexity of legal issues and the ease with which Hong Kong attorneys navigate through them.

This book, which is edited by James Kwan and Christopher To, weds the wealth of Hong Kong’s construction arbitration expertise with practical tips on how to avoid disputes or bring them to resolution. This book is particularly timely in 2015, when the shape and structure of the construction arbitration industry in Hong Kong is shifting from that adopted in the 1980s to a more competitive modern environment. Christopher To contributes to the treatise his extensive arbitration experience as one of the longest-serving Secretaries-General of the HKIAC, as well as the skill and know-how that comes with his role as Executive Director of the Construction Industry Council. James Kwan, a partner in Baker & McKenzie’s Dispute Resolution Group in Hong Kong, has guided his clients through the intricate labyrinths of construction arbitration for many years; he aptly summarises his counsel and arbitrator experience in this treatise.

The book comprises a collection of twelve chapters authored by some of Hong Kong’s most experienced construction practitioners. It includes twelve pages of appendices which contain useful forms regarding arbitrator appointments and examples of Scott Schedules, plus over twenty pages of case summaries and references, as well as a list of the relevant legislation.

Christopher To co-authored the first chapter with Julian Cohen, introducing the principles and the use of construction arbitration in Hong Kong. It is a foray into the history and the legal framework of construction disputes in Hong Kong. Phillip Rompotis, a partner in the Hong Kong office of Stephenson Harwood, authored the second chapter of the treatise, dealing with the nature of construction arbitration in Hong Kong and its early and progressive use. Paul Starr, a King & Wood Mallesons disputes partner, authored the third chapter dealing with the role of the HKIAC in the resolution of construction disputes in Hong Kong and its way several other Asian institutions deal with construction disputes. Timothy Hill, Hogan Lovells’ head of projects...
and the author of the fifth chapter, deals with several issues relating to arbitral appointments in construction disputes. Peter Clayton SC covers the commencement of construction arbitration in the sixth chapter, and Glenn Haley of Haley & Co deals with the jurisdiction and powers of the arbitral tribunal in the seventh chapter. Steven Yip of Minter Ellison contributes advice on case preparation, which includes considerations relating to preliminary conferences, Scott Schedules, witness testimony, and many other topics in the eighth chapter. The ninth chapter, authored by KK Cheung of Deacons, deals with interim and partial hearings, documents-only arbitration, multi-party arbitration, adjournment, costs and many other issues. The tenth chapter, which is contributed by Gary Soo, a barrister and a chartered engineer, is dedicated to arbitral awards in construction arbitration (final, interim, partial, consent, and additional or corrective). The eleventh chapter, which focuses on the recognition and enforcement of construction awards, is also contributed by Gary Soo. Finally, Vincent Connor and Mohammed Talib, both of Pinsent Masons, present their observations on the future of construction disputes in the twelfth chapter, where the reader may also find references to mediation and adjudication.

The contributing authors certainly turn the treatise into a guide on ‘Who’s Who in construction arbitration in Hong Kong’. Both the authors and the General Editors merit recognition for their labours. This treatise is indeed a useful practical guide and comes highly recommended to anybody wishing to possess a simple and straightforward guide to construction arbitration in Hong Kong written by those in the know.

Enforcement of Investment Treaty Awards: A Global Guide1

Reviewed by Nils Eliasson

The International Centre for Settlement of Investment Disputes (ICSID) is the world’s leading institution devoted to international investment dispute settlement. ICSID was established in 1966 by the Convention on the Settlement of Investment Disputes between States and Nationals of Other States (the ICSID Convention). As of 31 December 2014, ICSID had registered 497 cases under the ICSID Convention.

Some 64% of all ICSID cases have resulted in an award, whereas 36% have been settled or otherwise discontinued. In 46% of the cases that have resulted in an award, arbitral tribunals have upheld claims in part or in full. In these cases, recognition and enforcement of the award pursuant to the self-contained enforcement mechanism of the ICSID Convention could, however, potentially be an issue.

The same applies with respect to recognition and enforcement of non-ICSID investment treaty awards, pursuant to the New York Convention (predominantly investment arbitrations conducted under the UNCITRAL Arbitration Rules, the ICSID Additional Facility, and the Arbitration Rules of the Stockholm Chamber of Commerce).

Despite the importance of effective means of enforcing investment treaty awards, the topic has not attracted as much scholarship as various procedural and substantive issues that frequently arise in investment arbitration cases. One reason for this might be that investment treaty awards are often complied with voluntarily by the

3 See, for example, http://www.info.gov.hk/gia/general/201308/30/P201308300436.htm.
respondent States once available remedies against such awards have been exhausted. That being said, effective enforcement of investment treaty awards remains important and Enforcement of Investment Treaty Awards: A Global Guide provides helpful insights to practical aspects of the enforcement of both ICSID and non-ICSID awards in various jurisdictions.

The Guide is divided into two parts. The first part covers general enforcement issues such as ‘the origins and specificities of the ICSID enforcement mechanism’ and the important topic of ‘sovereign immunities and investor-State awards’, which generally represents the most difficult hurdle for the efficient enforcement of investment treaty awards in cases where the respondent State does not comply voluntarily. The different contributions in the first part are authored by representatives of ICSID and academics, as well as by practitioners.

The second part of the Guide provides an overview of rules relevant to the enforcement of investment treaty awards in certain jurisdictions, with an aim of highlighting specific issues or hurdles that may face an award creditor in the course of the enforcement of investment treaty awards in these jurisdictions. The different country surveys in the second part are authored by practitioners from various law firms with a connection to the jurisdiction in question.

The strength of the Guide is that it attempts to give a comprehensive roadmap for the enforcement of investment treaty awards under the ICSID Convention as well as under the New York Convention, including procedural issues and formal requirements that may face the award creditor in various jurisdictions. As is often the case with this type of guide or jurisdictional overview, however, the Guide would have benefited from a higher degree of editing. There is considerable repetition in the second part of general matters already addressed in the first, while some of the contributions in the second part go into considerably more depth than others.

That being said, this does not detract from the fact that the Guide represents a welcome contribution to the investment arbitration library.

Invitation to Submit Articles for Publication in the Asian Dispute Review

The Asian Dispute Review journal seeks articles with an Asian focus on arbitration, mediation and other forms of ADR. We are also pleased to receive commentaries, case studies, book reviews, and regional updates from around Asia.

If you are interested in contributing, please note the following guidelines:

• Contributions should be written in a style that is easily understood by lay readers.
• Contributions should not focus on substantive law, although brief comment on substantive law may be included to the extent that it adds to the understanding of arbitration and ADR.
• Contributions should not have been previously published in or submitted to another journal or news letter for consideration, and should not be available online.
• Contributions should not be on a subject covered in depth by any paper in the previous two issues of Asian Dispute Review.
• Contributions should in general be around 2,000 - 2,500 words in length, and must not exceed 3,000 words.

Before writing or submitting an article, we recommend that you read a complete version of our Submission Guidelines on www.asiandr.com – Submit a Paper, and contact the Editors first.

Please contact the Editors at asiandr-editor@hkiac.org if you have any submission enquiries.

Reports of events

HK45
HK45 held its Arbitration Update for 2015 seminar at HKIAC on 6 May 2015.

A specialist panel moderated by Robert Rhoda discussed recent arbitration developments in particular areas of the Asia Pacific region.

Tomas Furlong began with Hong Kong, dealing primarily with the Astor Lippo enforcement saga before the Hong Kong courts. He pointed out that although the arbitral tribunal did not have jurisdiction over the respondent, enforcement of the award was still allowed. It was said that, as Lippo did not act in good faith, it could not seek to resist enforcement.

Mr Furlong discussed active and passive remedies against awards and concluded that, given the current situation, it was advisable to exercise set aside rights immediately at the seat. The decision is currently under the appeal.

Matthew Hodgson discussed several points of interest arising from the Yukos case (in which record damages of US$ 50 billion were awarded). This case saw an interesting development in tax-related claims in investor-State arbitration.

Whilst the Energy Charter Treaty (ECT) covers expropriation, it does not cover taxation measures. The crucial question to be answered is whether taxation amounts to expropriation in each individual case.

Mr Hodgson emphasised that the ECT has no “doctrine of unclean hands”. Russia objected at the jurisdiction phase that there had been no investment as the subject arrangement was illegal. The tribunal reduced the remedy to Yukos by 25% at the end, recognising that there had been a breach of law in the form of tax evasion. The ‘elephant in the room’ was enforcement, the outcome of which remained to be seen. The claimants may choose to pursue Rosneft, claiming that it is the State; such action would, in fact, constitute a next step in the whole saga.

Desmond Ang shared with the audience recent developments from Singapore, particularly the establishment of the Singapore International Commercial Court (SICC). He explained the reasons for launching this court and discussed why the parties should choose it for the resolution of their disputes. Because the SICC is structured as a part of the Supreme Court of Singapore, it can enjoy the advantages of international treaties signed by Singapore, particularly those with common law jurisdictions with regard to reciprocal enforcement. The SICC has jurisdiction over matters of an international and commercial nature.

Mr Ang also discussed appeals from the SICC, suggesting that it was open to parties to agree on restricting or amending the right of appeal. Before choosing the SICC, parties should consider the question of enforcement of judgments. Whilst the New York Convention would not apply, enforcement under a number of mutual enforcement arrangements (discussed above) would be available. Finally, Mr Ang said that it would be open to foreign counsel for an “offshore case” to represent parties before the SICC.

Janie Wong gave an update on recent arbitration developments in India. She stated that delays and the interventionist approach of the Indian courts was slowly changing under the Modi government, which had promised judicial reforms.

Ms Wong stated that the number of cases in which courts intervened was also likely to drop because parties were increasingly using institutional arbitration. Ms Wong devoted the second part of her presentation to related institutional developments, discussing the LCIA (which had adopted a set of arbitration rules that were specifically applicable to India), the SIAC (which had opened a Mumbai office but not adopted any special set of rules), and the HKIAC (which had also become very active in the region).

Shi Lei summarised the controversy within CIETAC that had led to the breaking away of its Shanghai and Shenzhen sub-commissions in 2012, and was followed by the Chinese Supreme People’s Court interpretation in 2013.

Mr Shi noted that all cases so far decided included CIETAC arbitration clauses in contracts signed before the breakaway. However, there had as yet been no decision on the effect of arbitration clauses in newer contracts. He concluded by sharing tips on what to include in future arbitration clauses. It would be advisable to apply to CIETAC Beijing headquarters, specifying Shanghai or Shenzhen as a venue if desired, or using the proper up-to-date names of the new Shenzhen and Shanghai arbitral bodies if that was what clients wanted.

The concluding address was given by Joe Liu, who gave the HKIAC’s perspective on latest arbitration developments. Mr Liu asked a provocative question, “Why does it matter to be innovative?”, and proudly shared with the audience that the HKIAC had received the GAR Innovation Award for 2014. A new model arbitration clause had been adopted which included a choice of the governing law of the arbitration agreement itself.

In Mr Liu’s view, this was especially important in cases where the substantive governing law and the law of the seat were different. The HKIAC had also introduced its Guidelines on the Use of a Secretary to the Arbitral Tribunal and was offering tribunal secretarial services. Finally, Mr Liu informed the audience that the HKIAC had updated its rules for administering UNCITRAL arbitrations. These rules were unitary, in the sense that
they would govern arbitrations under any version of the UNCITRAL Rules that was applicable to a particular case.

**CIETAC mock Emergency Arbitration proceedings**

The China International Economic and Trade Arbitration Commission Hong Kong Arbitration Center (CIETAC-HKAC) delivered the first of several mock emergency arbitration proceedings (the mock proceedings) with the assistance of some of Hong Kong’s leading practitioners.11

The mock proceedings were held at King & Wood Mallesons’ Hong Kong office before a full audience, which included practitioners from local firms, barristers and in-house counsel.

Those participating in the mock proceedings were Mr Paul Starr, a partner at King & Wood Mallesons, who conducted the proceedings as the emergency arbitrator. The proceedings involved a fictitious mining trade dispute between two parties. Mr Cameron Hassall (Clifford Chance) and Ms May Tai (Herbert Smith Freehills) performed the role of counsel for the respondent. Mr Matthew Townsend (Norton Rose Fulbright) presented the application for emergency interim relief on behalf of the claimant.

Emergency arbitration has become an exciting recent development in international commercial arbitration and practitioners are beginning to appreciate the practical benefits it may offer to commercial clients. The emergence of the practice in Asian dispute resolution has been exemplified in the Hong Kong SAR as a result of amendments made by ss 22A and 22B of the Arbitration Ordinance (Cap 609).

The mock proceedings were designed to display the new Emergency Arbitrator Procedures available under CIETAC’s Arbitration Rules (2015 Edn)12 and their administration by CIETAC-HKAC. The response of the audience to the outstanding performance of the participants is a testament to the quality of the mock proceedings and the work that CIETAC-HKAC invested in it.

Similar mock proceedings took place in Guangzhou on 19 June 2015. Further such sessions will be held in Shanghai, Beijing and Seoul later in 2015. 13

**Arbitration law reform in Russia**

**O**n 6 August 2014, the Supreme Arbitrazh Court of the Russian Federation ceased to exist and its judges were dismissed. The Court was in charge of the recognition and enforcement of awards as well as of other arbitration-related matters in Russia. Its functions were transferred to Russia’s Supreme Court. In the light of that transfer, a number of legislative acts were adopted to adjust the structure and composition of the Supreme Court to accommodate these changes. A special Judicial Collegium for Commercial Arbitration was formed within the Supreme Court, comprising 30 newly appointed judges. Justice Ivanov, the former President of the Supreme Arbitrazh Court, is not among the new appointees. The Constitution of the Russian Federation and other relevant acts were amended to delete all references to the former arbitration authority.

Although major, this change is not, however, the end of Russia’s legislative reform. The April 2014 issue of *Asian Dispute Review* reported on the official opening by the Russian government of public consultations seeking input from the arbitration community on further legislative initiatives in the field of arbitration in Russia.13 In July 2014, the Legal Department of the Administration of the President of the Russian Federation returned the drafts so prepared to the Ministry of Justice for reconsideration.14 Almost a year later, on 7 May 2015, the Government of the Russian Federation submitted a revised set of laws to the State Parliament for approval.

The revised set of laws contains proposed amendments to the following legislative acts:

1. the Code of Arbitral Procedure;
2. the Code of Civil Procedure;
3. the Code of Criminal Procedure; and

The proposed amendments to arbitration laws redefine the courts’ supervisory function over the arbitral process, expand the scope of non-arbitral disputes, limit the jurisdiction of *ad hoc* tribunals, reduce the timeframe for domestic courts to decide recognition and enforcement applications, and allow retired judges to accept arbitral appointments.

One of the most important amendments relates to *ad hoc* arbitration. It appears that Russia is about to adopt the Chinese approach of excluding *ad hoc* arbitration from the list of recognised types of arbitration. If this amendment is adopted, the validity of *ad hoc* arbitration clauses in Russia would
be compromised. In its cover note to the proposed amendments, the Government explains that this particular amendment is introduced to “avoid abuse of this type of arbitration”. It is suggested that ad hoc tribunals will lose jurisdiction over corporate and shareholder disputes, and that domestic courts will be prohibited from supporting ad hoc arbitral proceedings.

Further amendments include a requirement that certain types of corporate and shareholder disputes may be referred to arbitration only if (1) the arbitral proceedings are seated within Russian territory, and (2) such disputes are administered by a recognised arbitral institution under a publicly available set of procedural rules. Another prerequisite to submission of such disputes to arbitration is that, in the case of multiple shareholders, both the company and all its shareholders are to demonstrate that they are bound by an arbitration agreement. Such corporate and shareholder disputes include those:

(1) relating to ownership titles to shares, related liens and encumbrances and other related rights;
(2) arising out of shareholders’ agreements and relating to election or termination of the mandates of corporate directors; and
(3) arising out of corporate management decisions.

At the same time, it is suggested that the following categories of dispute are to be treated as non-arbitrable:

(1) those relating to the exclusion of shareholders from corporate registers; and
(2) those relating to the acquisition of over 30% of shares of open joint stock companies.

Other amendments include changes to the Code of Criminal Procedure to recognise, on a statutory level, arbitrators’ immunity with regard to circumstances of which they may become aware during the arbitral process.

The revised set of amendments reaffirms that Russian courts are not to conduct a de novo review of foreign arbitral awards in the context of motions for recognition and enforcement. The statute of limitations fixes a period of one month in which to appeal against recognition and enforcement decisions of the lower courts.

It is expected that, if adopted, the amendments will enter into force on 1 September 2015.

Enhancing Hong Kong’s Position as a Leading International Arbitration Centre

Management consultancy KPMG was commissioned in August 2014 by the Hong Kong Trade Development Council, with the support of the Department of Justice, to carry out a study on enhancing Hong Kong’s position as a leading international arbitration centre in the Asia-Pacific region. In June 2015, following a round of initial interviews with practitioners and other interested parties, KPMG issued The Hong Kong Arbitration Survey, an empirical survey aimed at gauging Hong Kong’s strengths and competitiveness in this regard. Providers of arbitration services, practitioners, users and others are invited to complete the survey, which is available online.

Adjudication in Hong Kong

As foreshadowed in the October 2014 issue of Asian DR, the Development Bureau has published a Consultation Document (the Document) entitled Proposed Security of Payment Legislation for the Construction Industry. The Document, which stems from the discussions of a Working Group comprising construction industry stakeholders and Hong Kong Government representatives, seeks views on Security of Payment Legislation (SOPL) aimed at encouraging fair payment and rapid dispute resolution under construction and related contracts in both the public and private sectors. Comments on the Document should be submitted by 31 August 2015.

New arbitration rules

The International Institute for Conflict Prevention and Resolution (CPR) has issued a new set of Rules for Administered Arbitration of International Disputes (the 2014 Rules). The new rules, which took effect on 1 December 2014, are intended to reflect best international practice and are influenced by (inter alia) the work of UNCITRAL. They address a number of current issues in international commercial arbitration, including the length of arbitration proceedings, the impartiality of arbitrators and unpredictable administrative costs and requirements. In line with other new and emerging rules, the 2014 Rules provide for emergency arbitration by a ‘special arbitrator’.
Arbitration in Australasia

The Chartered Institute of Arbitrators Australia and the Arbitrators’ and Mediators’ Institute of New Zealand signed a memorandum of understanding in late April 2015 under which both institutions will encourage the use of arbitration for cross-border disputes. The memorandum follows the conclusion in 2014 of the ASEAN-Australia-New Zealand Free Trade Agreement, which will create a demand for cross-border dispute resolution services.

In a speech (as yet unpublished) delivered on the 30th anniversary of the foundation of the Australian Centre for International Commercial Arbitration (ACICA), the Chief Justice of the High Court of Australia, Robert French AC, stated that Australia was well placed to participate in the highly competitive market for dispute resolution services in the Asia-Pacific region. Despite the country’s geographical isolation in the region when compared with Hong Kong and Singapore, a number of other factors placed Australia in a position to become a regional international arbitration hub, particularly for disputes between US corporations and their Asian counterparts. These included the statutory framework, which implemented the UNCITRAL Model Law, the existence of ACICA and Australia’s “quality judiciary”.  

Investor-State arbitration

ICSID Annual Report 2014

ICSID has published its Annual Report for the fiscal year 1 July 2013-30 June 2014. In addition to providing a short guide on the ICSID investor-State arbitration process, the report provides statistics on ICSID arbitration. The period under review saw 38 new ICSID Convention cases registered, along with 2 Additional Facility arbitration cases. The total number of cases under administration during this period was 279, a new record, representing 44% of the 473 cases administered since ICSID’s inception. Bilateral Investment Treaties (BITs) and the Energy Charter Treaty (ECT) provided the basis of consent to arbitrate in 49% and 22% of cases respectively. With regard to geographical distribution of the total cases registered, by host State, South and East Asia and the Pacific accounted for 3% of them and Eastern Europe/Central Asia 25%. The report also features information about (1) economic sectors involved in ICSID cases, (2) outcomes in ICSID arbitration and conciliation proceedings, including outcomes to date in annulment proceedings under the ICSID Convention, and (3) the nationalities and geographic origins of arbitrators, conciliators and ad hoc committee members appointed in ICSID cases.  

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1 A group of young professionals formed under the auspices of the Hong Kong International Arbitration Centre (HKIAC).
3 Editorial note: See Yukos Universal Ltd (Iste of Man) v Russian Federation, PCA Case No AA 227, Final Award.
7 Editorial note: See HKIAC India Road Show [2013] Asian DR 35.
8 Global Arbitration Review.

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News section contributors:

Olga Boltenko
Michal Čáp
Robert Morgan
Joshua Storey
Brad Wang

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<td>Hong Kong International Arbitration Centre</td>
<td>Vis East Moot Foundation Ltd</td>
<td><a href="http://www.cismoot.org/docs/events/2015%20YIMC%20Competition%20Rules%20Final.pdf">http://www.cismoot.org/docs/events/2015%20YIMC%20Competition%20Rules%20Final.pdf</a></td>
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<td>IBA Annual Conference 2015</td>
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<td>HK Arbitration Week:</td>
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<td>• UNCITRAL Asia-Pacific Judicial Summit</td>
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<td>24 NOVEMBER</td>
<td>3rd International Arbitration Conference</td>
<td>Harbourside Room, Museum of Contemporary Art, Sydney</td>
<td>Australian Centre for International Commercial Arbitration (ACICA), the Business Law Section of the Law Council of Australia (BLS) and the Chartered Institute of Arbitrators Australia (CIarb)</td>
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<td>10 DECEMBER</td>
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<td>Hong Kong Club, Hong Kong</td>
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Contributed by Ms Karen Tan (HKIAC)
LOCAL ROOTS  GLOBAL IMPACT

"The only local arbitration commission which meets or surpasses global standards" - The Economist Intelligence Unit

"Professionalism, competence and transparency" - Global Arbitration Review

BAC/BIAC Profile
The Beijing Arbitration Commission (BAC), also known as the Beijing International Arbitration Center (BIAC), was established in 1995 as a non-governmental arbitration institution, and became the first self-funded Chinese arbitration institution in 1999. It provides institutional support as an independent and neutral venue for the conduct of domestic and international arbitration and ADR proceedings. It is operated by a Secretariat headed by its Secretary General under the supervision of its Committee. The BAC/BIAC Arbitration Rules 2015 were unveiled on December 4, 2014, and came into force on April 1, 2015. The 2015 rules widely accept UNCITRAL Arbitration Rules and further accept up-to-date international practice.

BAC/BIAC Growth
- From 7 cases filings in 1995 to over 24,000 cases in total by 2014
- 1500+ new filings on average per year since 2005
- 600+ international cases in total
- Parties from various jurisdictions including USA, UK, Germany, Australia, Japan, South Korea, Singapore, Hong Kong and Taiwan, etc.
- The sum in dispute of around 11.1 billion RMB (approx. 1.8 billion USD or 1.7 billion EUR) per year on average since 2010 with a highest claim amount of 10 billion RMB (Approx. 1.52 billion USD or 1.48 billion EUR) in 2015

Recommended BAC/BIAC Model Clause:
All disputes arising from or in connection with this contract shall be submitted to Beijing Arbitration Commission / Beijing International Arbitration Center for arbitration in accordance with its rules of arbitration in effect at the time of applying for arbitration. The arbitral award is final and binding upon both parties.
11-12 November 2015  Marina Bay Sands, Singapore

STEP ASIA CONFERENCE 2015

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Programme focus:
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- Educating New and Existing Clients on Exchange of Information (EOI) to Automatic Exchange of Information (AEOI)
- Divorces – Shopping for a Jurisdiction
- Private Trust Company & Family Office (PTC): The Trends for the Future – Good, Bad and Unknown

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Improving Your Arbitration Presentation
With a Mock Arbitration: Two Case Studies
By Edna Sussman

“Who speaks to the instincts speaks to the deepest in mankind, and finds the readiest response.”
Amos Bronson Alcott, American Educator and Philosopher (1799-1888)

With the recent blitz of scholarly and popular works on the science of judgment and decision making, attention has begun to focus on the decision making of arbitrators. Arbitrators are people and like all people have their own frames of reference, experiences and societal inputs that guide their thinking and their decision making processes. Indeed it is precisely because arbitrators are not all the same that many have argued that the party-appointed system for arbitrator selection is a sine qua non if arbitration is to prosper. While legal principles and precedents are an overlay that clearly influences final decision making by arbitrators, subconscious factors that inevitably influence every person also play a significant role. Thus a party’s selection of the arbitrator most likely to come into the arbitration with unconscious predilections favorable to that party’s position can be an important factor in maximizing the chances of winning. Similarly, counsel’s framing of the dispute and the theme developed to tell the story to evoke a positive response from the arbitrators is known by all to be essential to a persuasive presentation.

The routine employment of jury consultants is a response to the importance of selection and messaging. However, the arbitration community is just beginning to explore how counsel can strategically respond to arbitrators’ inherent frames of mind. These discussions and explorations have led those versed in the fields of psychology and arbitration to conclude that “the most useful scientific tool we have in preparing for an arbitration hearing is a mock arbitration panel study.”

The mock arbitration will not suffer from what is known as the “good subject” response or from confirmation bias, unlike vetting with colleagues at the firm or with an arbitrator hired as a consultant to advise on procedure or strategy. Rather, independent arbitrators similar to those who will actually hear the case will evaluate themes and facts without knowing which party is presenting. These neutrals can provide a road map (with the aid of social scientist consultants) on such matters as how to refine or revise the theme developed to tell the story more sympathetically, which legal theories to emphasize, whether particular kinds of graphics would be helpful and what kind of expert explanations would be most useful. Recalibration of the case based on these insights should result in the most persuasive presentation to the real arbitrators. If social science tools are used early in the process to assess potential arbitrators, they can also serve to assist in the selection of arbitrators more likely to be receptive to the party’s submissions.

The use of mock arbitrations to enhance the likelihood of successful outcomes in larger cases is likely to grow significantly in the coming years as those in the arbitration community become more familiar with the availability of these tools and their benefits. The globalization of commerce and the increased participation of arbitrators from many different cultures is likely to make such a process even more valuable as counsel seek tools to assess how best to persuade arbitrators with different backgrounds.

There are many different system designs for a mock arbitration process and each process must be crafted and tailored to the specifics of the case. I offer vignettes from my experience with mock arbitrations as examples of two system designs. Both were orchestrated by consultants well-versed in developing appropriate protocols with years of experience employing these social science tools in other litigation contexts as well as increasingly in arbitration.

"The use of mock arbitrations... is likely to grow significantly... as those in the arbitration community become more familiar with the availability of these tools and their benefits."

The Matching Surrogate Panel Model

The call came from an ADR consultant: can I serve as a surrogate arbitrator to participate in a one-day mock arbitration in Washington, D.C. in a multi-million dollar dispute? I was told that I was selected as a good match for one of the arbitrators in the real arbitration. Two others had also been chosen as good matches. We were not told who the real arbitrators were or what factors were considered in our selection. All of us had been suggested by one of the arbitral institutions as fitting the characteristics provided of the real arbitrators along with others who were reviewed by the consultant before our selection was made.

After signing a very stringent confidentiality agreement, the three of us were given materials to prepare. To control costs we were told to limit our review of the papers to 5 hours. We were also asked to respond to a short series of questions to gauge our initial reactions. The mock arbitration followed at a law firm’s offices. We were not told which side of the dispute that law firm was representing. I was asked to chair the panel. Lengthy arguments by both sides were presented with power point presentations.
We were asked to hold our questions to the end. The room had a see-through wall on one side so that the consultant and others could observe the proceedings.

Following the argument, and without conversing, we were asked to respond to another set of written questions and then were offered the opportunity to ask counsel questions. Panel deliberation followed and was observed through the one-way see-through wall. We came to a consensus relatively quickly and counsel came in, debriefed us and sought reactions to various strategy options, including such fundamental questions as which legal theories to pursue and whether some should be dropped, whether the industry witnesses they were planning to use would be persuasive and how to deflect some troublesome facts. A lengthy productive dialogue between the surrogate arbitrators and counsel completed the day.

Subsequently the lawyers called me to tell me that the mock arbitration had been very helpful to them. There ensued a more traditional consultation process with counsel seeking guidance from me as an arbitrator but in this case as an arbitrator who had been selected by the ADR consultant as a match for one of the real arbitrators. I was asked to review the initial prehearing submissions, both the briefs and the very extensive fact and expert witness statements, so that I could advise them as to what I thought was most important to rebut and what to highlight in the reply papers. A consultation session followed to review my recommendations and to try to predict how the real arbitrators might react on specific issues. Subsequent consultation sessions were held to discuss how to present the evidence most persuasively, which witnesses to emphasize and in what order, how to allocate time in what was to be a chess clock arbitration, and other strategic and practical hearing considerations.

The Multiple Arbitrators Model

Another call came from an ADR consultant asking if I could serve as a mock arbitrator in a one-day session. This time I was to be one of about 40 arbitrators gathered from around the country to participate in the mock arbitration hearings. The case concerned a structured financial product with respect to which I gathered there was an expectation of many claims being brought. The confidentiality agreement, again one of the most stringent I had ever seen, required a commitment not to take any arbitrations subsequently involving that specific structured product.

Forty of us gathered in midtown Manhattan where we had breakfast and were presented as a group with a one-hour presentation on the basic facts of the case using facts as they related to a single fictional investor. We were not given any materials in advance. Unlike the first mock arbitration, it was pretty easy to guess that it was the company which sold the financial product that had brought us together.

We were divided into panels with 5 arbitrators on each panel and seated in 8 separate rooms, each with a one way see through wall. Lawyers, we later learned from different firms, presented their arguments for the defense. We were permitted to ask questions but were asked not to limit them in order to allow time for the lawyers to present their arguments.

Panel deliberation followed, again observed through the one way see through wall. After consensus was reached, we were debriefed by in-house counsel for the respondent both as to our views of the merits of the case and various specific facts and arguments made by counsel.

We learned that the mock arbitrations were being used for several purposes. It was a beauty contest for 8 law firms competing for the business of defending the expected hundreds of claims. Each lawyer had independently developed his or her own approach to the defense. Performance and success at persuasion at the mock arbitration was to play a major role in the selection of counsel. The mock also served the more traditional purposes of identifying the most successful strategy and assisting in analyzing the settlement values that would be appropriate for the claims.

Conclusion

As we strive to maintain arbitration as a more streamlined process than litigation, the value of the case is an important consideration in determining whether embarking upon a mock arbitration process is indicated. However, with the growth of high value arbitrations in recent years, the additional expense incurred in a mock arbitration may well be justified in particular cases. We can expect that parties and counsel will increasingly avail themselves of this process for improving their odds of winning as information about the possibility of mock arbitrations and their utility becomes more widely known.

Endnotes

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The Social Science Edge in Arbitration and Mediation
By Dr. Philip K. Anthony and Les J. Weinstein, Esq.

The value added by jury consultants has long been recognized by the trial bar and has led to an explosion in the use of such assistance to maximize the chances of winning. While the tools and methodologies differ, dispute resolution consultants can bring their skills and experience to bear to help counsel identify surrogate arbitrators, design a mock process, assess their real arbitrators' likely reactions and help develop an optimally persuasive presentation of the case. Counsel who have employed such assistance in arbitrations have found the input most useful. We review here the growing field of domestic and international dispute resolution consulting.

The Use of Social Science Research in the Legal Arena

The disciplines of the social sciences have been successfully and consistently applied to the field of courtroom litigation for forty years, beginning most noticeably with the trial of the "Harrisburg Seven" in 1972, when for one of the first times, social scientists applied their craft to assist lawyers and litigants in studying and usefully applying juror behavior in a trial environment. The social scientists and trial lawyers asked themselves a few deceptively simple questions: How might juror attitudes and experiences from their own lives impact their views in this prominent trial? What elements of the trial facts are fairly well understood, what parts are misunderstood, and overall, what specific elements of the trial work in concert to shape, guide, and help form the thinking and evaluation of the trial and its correct outcome in the minds of jurors as the triers of fact?

The disputed issues and facts which are presented are often boiled down by jurors to those which best resonate and fit in with their personal life experiences. The task of counsel is to use that derived research information to either confirm or challenge those juror predispositions. Ultimately, this form of research and analysis was also applied equally effectively to bench trials where the trial judge, though steeped in the law, is in effect a jury of one as the trier of fact.

As it turned out, and as the reader may have personally experienced, the systematic study of the decisions of surrogate and actual jurors and those of trial judges, when analyzed for the purpose of understanding how they process information presented at trial, has been dramatically refined and improved over the years and can effectively enhance, sometimes dramatically, trial presentation strategy—often giving lawyers a convincing communications edge. Lawyers frequently report that they believe that such research was likely outcome determinative. Post-trial interviews of actual jurors confirm the value of such research in laying down psychological anchors in the minds of decision makers. Often it is a testament to the power of words and concepts. As Mark Twain is reputed to have said, "The difference between the right word and almost right word is the difference between lightning and a lightning bug."

At its core, what is it about the process that allows for success? There are several correct ways to analyze this question, but most fundamentally, people everywhere and across cultures generally make decisions in a relatively consistent manner by taking into account their own attitudes, principles, background, values, cultures, and experiences gained during a lifetime and applying them to evaluate a set of facts and in which there is a dispute between two or more parties. By systematically studying and observing such human behavior, it is now very often possible to discern a pattern by which people will reach decisions in particular disputes and to make reasonable educated assumptions about those decisions and how they may be altered by what is presented and how it is presented.

Arbitrators Are People Too!

Whether your case is being heard by a jury, a trial judge, an arbitrator, or is being mediated, people are people. Even "neutrals" striving to be fair minded will have a world view, a cultural and legal frame of reference, biases, prejudices, and predispositions like everyone else. The role of the dispute resolution consultant is to anticipate any adverse predispositions and to solidify views favoring the client. Fast-forward to the present, and it can be observed that fundamental social science concepts and techniques are now being applied to the dispute resolution world of both arbitration and mediation. A fter all, just as the decision making of jurors and trial judges can be studied and evaluated, so too can that of dispute resolution neutrals. The result may be beneficial to the party choosing to investigate and apply the social science findings to the arbitration tribunal—whether composed of three neutrals or single decision making arbitrator—or even a decision influencing mediator.

There are a number of ways this research exercise can be structured and conducted which are case specific and may be cost- and time-bound. A assistance may be given as early in the process as the selection or rejection of the actual neutrals. Counsel often complain that they have insufficient information about the neutrals they consider. Compounding this dearth of information is an absence of the application of the kind of social science analysis...
of predispositions that lawyers have found so helpful in jury selection. In a large case, such extra assistance during the neutral selection process may be well worth the additional expense. After all, counsel generally seek an impartial and independent arbitrator but one that has a predisposition that is favorable to their side of the case. The dispute resolution consultant will work with the advocates to help identify likely predispositions and beliefs held by the neutral. Once the arbitrators are selected, there are a multitude of specific research techniques, but the most commonly followed methodology in an arbitration setting is to undertake what is sometimes called “mock” arbitration research.

The dispute resolution consultant recruits from the special community of experienced and case-appropriate surrogate neutrals, often from an already developed extensive database, one, three or more individuals who possess characteristics or background deemed to be most consistent with those of the actual or anticipated neutrals. By way of simple example, if one of the arbitrators already selected is a former law firm partner, one is a former judge and one an academic, each of a certain age and background with experience in specific relevant industries or special legal expertise, then surrogate neutrals are recruited with the same personal characteristics, business experience, educational background, skill set/qualifications in mind. While counsel may be tempted to try this on their own, it’s impossible to do so without having access to the neutrals or the social science background and grounding in the rigorous methodology required to make the study statistically reliable.

Importantly, in order for the study to be effective, it must be a “blind” study for the surrogate neutrals, meaning they are not specifically aware which side in the dispute has retained their services. Within the social science literature there exists a term of art known as “subject bias,” meaning if a subject (the surrogate neutral) knows the intent or sponsor of the study, he or she is likely to subconsciously or otherwise take that factor into account and filter responses and evaluation through that prism, resulting in a less than accurate collection of responses.1 Mock presentations to test strategy with one’s own colleagues at a firm, as many lawyers do, are likely to provide false positives and fail to provide the benefits equal to the matching of characteristics required and provided by those utilizing social science techniques.

It is essential that the design of the process be conducted in close harmony with the lawyers who will present the case. Many factors enter into structuring the research in addition to the surrogate neutrals themselves, including, for example, characteristics and presentation techniques of opposing counsel, the reputation of the parties, evidentiary presentation latitude, and the witnesses who will testify. If there are to be three arbitrators, the potential intra-panel dynamics are yet another and sometimes potentially outcome determinative factor to evaluate. The research is case specific, both as to the surrogate arbitrator(s) selected, the materials (and sometimes witnesses) presented to them and the manner of presentation. The stakes involved, the length of the actual proceeding, the nature of the legal issues, the status and position of the parties all play a role in structuring the study. A study designed for a routine domestic arbitration before a single arbitrator will be designed differently from a cross-border or international arbitration between multi-nationals heard by arbitrators from several nations who bring their own cultural backgrounds to the proceeding.

Typically the surrogate arbitrators participate in a mock hearing. The mock arbitration may be conducted in many ways. How extensive the materials provided to the arbitrators in advance of the mock session varies depending on the complexity of the case and the budget. A mock hearing generally truncated in length to reduce costs, follows before one, three or more arbitrators “sitting” alone or as members of a surrogate panel.

The output from such a research exercise usually takes the form of a report, detailing the specific individual reactions of the several surrogate neutrals as well as identifying the pattern and commonalities of response from all surrogate neutrals when they act as a panel. Lawyers tend to want to know if their evidence, concept of the case, and strategy were effective—rather than learning what evidence, argument, or strategy worked well. However, understanding the persuasiveness of the case as presented allows for modification of tactical or substantive presentation considerations for implementation at the tribunal, such as a change in emphasis or focus, better, more detailed demonstrative exhibits, the selection and use of experts and witnesses, and/or the introduction of a needed subject matter animated or filmed tutorial. Counsel will often learn through this process that there is a more efficient, dearer, and more convincing manner in which to position the issues in the dispute and how best to prepare or select witnesses and which documents to emphasize. This is particularly true where, as usual, there are presentation time constraints. In addition, there may be a valuable opportunity to “re-road test” a different approach to the case prior to the main event by using yet another surrogate panel to evaluate the changed strategy.

Mediators, Like Arbitrators, Are People Too!

Much the same may be said of the presentation in a mediation proceeding before a different kind of neutral who, while not having the power to decide, often has the power to persuade. In a mediation, counsel has a unique opportunity to structure the mediation statement and both the joint and caucus presentations—where there are few rules (other than confidentiality)—not only to the mediator but also, perhaps for the first time, to the opposing party and its counsel. The party presenting its case in a
provides guidance as to how to most efficiently and productively present a contested case to the actual neutrals to gain a presentation edge and enhance the chances of winning in arbitration or successfully settling the dispute at mediation.

Endnote
1. Referred to as the “good subject” role or response—the tendency of experimental subjects to act according to what they think the experimenter wants—in Experimental Psychology, Donald H. McBurney, Wadsworth Publishing Company, 1983.

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Conclusion
Litigators long ago learned the value of using consultants to help them apply the social sciences to court environments with both juries and judges to win cases. With increased focus on dispute resolution arising from trial costs, limited court budgets, slow trial processes, long appeal times, lack of confidentiality, and a global economy in which companies increasingly prefer arbitration or mediation and shy away from foreign court trial proceedings, the dispute resolution field is changing at an accelerated pace. Arbitration and mediation counsel, with increasing frequency, are today following with similarly useful processes. The application of social science research can be a valuable tool in the advocate’s toolbox.
Mock Arbitrations: Getting the Most Value for Your Project

By Stephen Tuholski, Ph.D.

Mock arbitrations, like mock trials, are useful tools for assessing and recalibrating litigation strategy. When conducted properly, the data from a mock arbitration project can significantly increase the chances of success at an arbitration proceeding. On the surface, conducting a mock arbitration appears to be a relatively straightforward process. Gather some arbitrators, present your case, and observe arbitrators as they discuss and reach decisions based on the evidence and arguments. In fact, an effective mock arbitration that provides strategic level insight and value can be effectively leveraged during your arbitration proceedings must be based on sound scientific methodology. Failure to rely on sound scientific methodology will result in a potentially disastrous “garbage-in garbage-out” scenario in which the data used to develop strategic recommendations are neither reliable nor valid. The best case scenario in these situations is that clients waste a significant amount of money on a project that produced results that were not helpful, while the worst case scenario results in an attorney relying on those results, much to the detriment of his or her client. In situations like these, it’s better to not conduct a research project than to conduct a poorly designed project. In the following article, I describe how best to increase the value and utility of your mock arbitration project.

"Consider the question 'at the end of this project, what do we need to know?' and design the project...”

A typical mock arbitration involves many phases, including recruiting arbitrators for the project, organizing and delivering materials for the arbitrators to review in advance of the mock arbitration, and the mock arbitration event, which includes the presentation of all relevant party’s evidence and arguments, arbitrator discussions/ deliberations, and a summary debriefing session with arbitrators. Before this process begins, the most important thing to do is to clearly define your goals for the research.

Goals and Expectations

More often than not, if you are considering a mock arbitration project, you are doing so because the potential monetary award is significant, and the facts and/or laws governing the matter are complex. Clearly, most arbitration matters either do not need to be tested in a mock arbitration, or even if there is a need, the cost-benefit analysis may not work in favor of doing a research project. As such, it’s likely that the types of matters that require a mock arbitration are those that would ultimately involve multiple days of argument from both sides during the actual arbitration hearing. Unless your budget is virtually unlimited, it will be impossible to present specific levels of detail for every single argument and fact that you would present during a real arbitration at a research project. Although multiple day mock trials are fairly commonplace, it’s rare that a mock arbitration lasts more than a day or two, because of the concomitant arbitrator fees associated with a longer project.

With this in mind, the first question you should ask is “What do I want to accomplish with this project?” The answers to this question may range from testing very specific arguments, to gaining a better understanding of your client’s financial exposure, to gaining a better understanding of what a “win” would be at arbitration. There is often disagreement within a litigation team as to what the goal of mock arbitration should be. The best way to limit the scope and goals of the mock arbitration project is to work backwards. That is, consider the question “at the end of this project, what do we need to know?” and design the project so that you can generate the most reliable and valid answers to those questions.

A mock arbitration will be more valuable if you limit your scope to the most important or vulnerable aspects of your case and not try to present a week-long arbitration in a single research day. You will find more value in your mock arbitration experience if you present a few key pieces of evidence and argument very well, rather than attempting the shotgun approach of presenting a little bit of everything in a reasonably short timeframe. In a typical one-day project, there may be five hours total for both party’s presentations, so that there is enough time for arbitrators to discuss and deliberate, as well as a chance to debrief the arbitrators. It’s important to remember that the value of the project stems from what the arbitrators have to say, and in a zero-sum time situation, the longer the attorneys use on their presentations, the less time there is for arbitrator feedback and data collection. More often than not, this process will leave arbitrators with their own questions, as they may recognize that certain evidence and arguments are missing, but it is better to work through these issues during a debriefing period than attempting to present everything in a short time frame.

In terms of expectations, the worst mistake you can make in a mock arbitration is trying to “win” the case. More important than “winning” your mock arbitration is learning where the warts are in your case, and learning where your adversary’s strength lies. As such, it’s critically important to make sure that both sides of the case are argued as effectively as possible. When arguing the other side of the case, put on your adversary’s best evidence and arguments, and present them with the same vigor as you would present your client’s position. During preparations for the mock arbitration, make sure both “sides” are com-
municating so that they end up presenting on the same or similar issues. If the Claimant attorney presents certain evidence that the Respondent attorney does not address, this can create dissonance and confusion with the arbitrators. Without hearing the best of both sides of an argument, arbitrators are unlikely to give proper feedback on that argument, and counsel can be left with dangerously invalid data and conclusions.

Oftentimes, the task of arguing the adversarial side of a case is put on an Associate at the firm or a more junior Partner, presumably because the lead attorney on the case wants to remain focused on her arguments. This is a mistake. Although it is often an uncomfortable proposition, it is more effective to have the lead attorney argue and present the adversarial side of the case. Doing so makes the attorneys more fully appreciate their adversary’s facts and arguments, and often results in the kind of insights that they would not get if they didn’t have to walk a mile in opposing counsel’s shoes. More often than not, counsel indicate that the simple process of putting together their adversary’s case leads to great insights that they otherwise may not have developed if they remained solely focused on their own case, a tangential but significant value of the mock arbitration process.

Witnesses and Graphics

Arbitrators will reach decisions not only based on their interpretation of the facts and law involved in the case, but also by their reactions to witnesses. For the purposes of a mock arbitration, there are three ways to present witness testimony: via reading their testimony into evidence from transcripts or in summary form, through the use of recorded video depositions, or by live witness testimony at the mock arbitration. Whenever possible, bring live witnesses to a mock arbitration and avoid reading in testimony. Although arbitrators are trained to be objective, it is unwise to dismiss the unconscious effects that occur when given the chance to observe a witness’s body language even though by definition we are not aware of some of those effects. It is infinitely better to identify a troubling witness (in terms of their body language and demeanor) during a mock arbitration project when there is time to work on their performance issues than at the actual arbitration when it is too late.

Similarly, a mock arbitration provides an excellent opportunity to test graphics that will be used at arbitration, particularly demonstratives that are developed for the purposes of explaining complex subject matter. Often we are easily impressed with our own attempts to represent complex ideas graphically because we have spent a lot of time with the facts, and as such it’s possible to overestimate the utility of our graphics. Learning how mock arbitrators react to, and develop opinions of, graphic representations is another way that a mock arbitration allows us to course-correct litigation strategy.

Number of Arbitrators

A common question asked about mock arbitrations is “How many arbitrators should we use?,” and the correct and often dissatisfying answer is, “It depends.” Mock arbitrations can be conducted with as few as one arbitrator, and as many (in the author’s experience) as twenty-five arbitrators. Although there is a natural desire to bring in as many arbitrators as possible, it’s important to consider the quality of the arbitrators as much as the quantity. If the real arbitration panel has already been selected, it is valuable to recruit mock arbitrators with similar background experiences and demographics. For example, in a FINRA arbitration, if counsel knows that the actual panel will be comprised of a non-public and two public arbitrators with real estate and construction experience, the project would benefit from recruiting arbitrators with similar background experience.

While using a single arbitrator is likely to yield some valuable data, including more arbitrators significantly increases the utility of the data. A mock arbitration that is used to test and understand a single matter in a single geographical location may be well served with a panel of three arbitrators, while mock arbitrations that test issues that may be occurring in several jurisdictions are clearly better served with a more diverse sample of arbitrators and more panels that represent those distinct jurisdictions.

In an ideal world, a mock arbitration would have two or more panels of three arbitrators each, and the process of the mock arbitration would include providing the same background information to each panel and then breaking the panels out for different presentations that represent different approaches to the case. In this way, it’s possible to test and analyze the efficacy of certain argumentative approaches in terms of relative and overall strategic value. One problem that is often overlooked in research is that if one wants to “test” an approach, the test should involve a comparison group. For example, if you believe that there are two fairly mutually exclusive approaches that you could take at the arbitration, one way to determine which is the better route is to present both at a mock arbitration, each to different panels. If only one approach is “tested,” there are no relative data to compare that approach to.

Summary

Not all mock arbitrations are created equally. With the proper guidance and insight into the process, a mock arbitration provides an opportunity to test and adjust various arguments, witnesses, and graphics, which ultimately increases your chances of success during the real arbitration.

Endnote


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Making the most of mock arbitrations

25 May 2017

Increasingly, international arbitration practitioners are using mock arbitrations – like mock jury trials in the United States – as a valuable tool to assess the strengths and weaknesses of a party's position and develop an effective way to present their case in the real arbitration. Claudia Salomon and Peter Durning of Latham & Watkins highlight what must be considered to ensure the exercise is calibrated to the needs of the case.

There is no one-size-fits-all approach to organising a mock arbitration but there are factors to consider – including who to place on the tribunal; what subject matter cover; when to hold the hearing and how to incorporate feedback.

There's also the big "why" – the strategic goals of the exercise.

By carefully tailoring the mock arbitration to the needs of a specific case, counsel can make the most of it. Here's what we think they should consider.

**WHO? Choosing your mock arbitrators**

A mock arbitration is a predictive exercise and, when selecting mock arbitrators, the overriding goal is to enhance its predictive value. In arbitration, the real arbitrators’ identities are known early in the proceeding, and the mock arbitrators are therefore selected to replicate the composition of the tribunal.

This process contrasts with mock jury trials in the US, in which the similarities and differences between the mock jurors and the real jurors cannot be assessed because the real jurors’ identities are unknown before trial.

As a result, a mock arbitration can have greater predictive value than a mock jury exercise, provided the members of the tribunal are carefully matched to mock arbitrators with similar profiles.
In some cases, cost considerations make it impractical to retain an external group of mock arbitrators. To reduce costs, it is possible to create a tribunal in-house, using partners from one’s own firm as the mock arbitrators, though this approach may result in a mock tribunal that is less candid and provides less critical feedback.

Overall, an exercise using in-house mock arbitrators is likely to provide a lower predictive value than an exercise in which mock arbitrators are selected based on closeness of fit with the real arbitrators.

When attempting to match a real arbitrator to a mock arbitrator with a similar profile, there are many factors to consider, including:

- Legal tradition and training;
- Nationality;
- Familiarity with cultural or business norms relevant to the case;
- Industry-specific expertise; and
- Age, gender, and language.

Typically, the candidate’s legal tradition and training is the most important factor – in a predictive exercise, the way in which an arbitrator thinks about procedure, contracts, and the equities is often the most useful dimension to model.

However, in cases where the primary driver of the parties’ dispute is a difference in cultural expectations (rather than legal opinions), a candidate’s familiarity with cultural or business norms can be even more valuable than a shared legal tradition and training.

In some circumstances, it is possible to find a mock arbitrator who personally knows a member of the real tribunal and claims an ability to predict his or her reactions. But it is difficult to determine how much weight to give to a mock arbitrator’s opinion based on a personal connection, just as it may be difficult to evaluate how well one person knows another. A close friend of a member of the real tribunal may have real insight into how the real arbitrator may approach issues. By contrast, a mere acquaintance is likely to have only limited predictive ability, unless he or she shares a similar profile with the real arbitrator or their connection includes service as co-arbitrators on a prior, similar case.

For these reasons, the most reliable course is to focus on similarities in the profiles of the mock arbitrator candidates and members of the real tribunal, rather than any personal connection between them.

The selection and retention of mock arbitrators raise certain practical questions: how should the mock arbitrator candidates be identified, approached, and retained? The process for identifying mock arbitrator candidates is similar to the process used to identify and nominate the members of the real tribunal, and involves consultations with one’s internal and external network of arbitration practitioners. Additional candidates may be found by considering the real arbitrators’ potential connections with former law partners or colleagues, former judges of the same court, or members of the same professional organisation or society.

When candidates cannot be found after an extensive search, it may be useful to seek the assistance of an outside company specialising in mock trials and arbitrations. These companies often can suggest candidates based on their own registries of practitioners. However, counsel must conduct their own diligence on those candidates, and should always personally contact candidates regarding service as a mock arbitrator rather than delegate that responsibility to an outside company.

Once the mock arbitrators have been selected, they must be formally retained. Counsel should structure the engagement letter so that the mock arbitrators are treated as “consultants” – a designation that may limit complications with disclosures the mock arbitrators may be required to make in future matters.

After the mock tribunal has been engaged, counsel should arrange for its members to meet to discuss the case between themselves in advance of the mock hearing.
What? Subject matter and structure of the mock arbitration

The scope, subject matter, and structure of a mock arbitration are often determined by the threshold question of resources – a mock arbitration can be long and detailed or short and focused, depending on the amount of money and time available for preparing and conducting the exercise. Within those bounds, however, the subject matter and structure of the proceeding can vary substantially, depending primarily on the following:

- The issues, arguments, themes, and evidence that counsel wishes to test;
- The type of practice required, whether oral arguments of counsel or presentation of witnesses;
- The identity of the lawyers who will participate in the mock exercise and their anticipated role at the actual hearing; and
- The degree to which the mock arbitrators have been asked to prepare for the exercise by reviewing the parties' written submissions and the record in the case.

The relative importance of these factors depends on the needs of the case and the reasons for conducting the mock arbitration.

In most cases, counsel should focus on selecting the issues that are the most substantively important and creating a strong draft of the presentation to be delivered on those issues at the hearing. Counsel can test the overall strength of the case by delivering a mock opening statement that covers all material issues, or alternatively, make modular presentations on discrete issues.

In a lengthy mock exercise, counsel can combine a comprehensive opening statement with a modular approach, resulting in a mock arbitration that is both broad and deep.

In certain circumstances, where permitted by law and ethical requirements, the mock arbitration may focus on preparing the witnesses for the hearing. In such cases, the mock arbitration offers the added benefit of familiarising a witness with the hearing process.

Counsel also may find a mock arbitration an effective means to prepare for cross-examination with a mock adverse witness. Overall, however, the mock arbitrators' time is usually best spent evaluating counsel's presentation of the issues – not the performance of a witness or a mock adverse witness.

Regardless of the substantive issues or type of presentation that counsel places at the centre of the mock arbitration, it is essential to present both sides of each argument, perhaps with a "blue team" representing the actual client, and a "red team" representing the adversary. Depending on the staffing, it may be helpful for the teams to work together or work in silos, more closely simulating an actual arbitration. In staffing these two teams, counsel should consider each lawyer's likely role at the hearing.

When possible, members of the “blue team” should have the same role in the mock arbitration that they will have at the real hearing. The “red team” can be a proving ground for the more junior lawyers who may be called upon as backup at the hearing; however, a robust presentation of the adversary's case should still be delivered so that counter-arguments and the mock arbitrators' feedback are both well developed. To that end, counsel may benefit from having one of the lead lawyers deliver the “red team's” presentation.

In structuring a mock arbitration, counsel must also consider what information to provide the mock arbitrators in advance, keeping in mind any confidentiality orders in the case. Generally, the parties' substantive briefing (including memorials and statements of claim or defence) should be provided, along with particularly important witness statements. To ensure that the mock arbitrators focus only on the most material submissions, counsel typically should not provide mock arbitrators with procedural orders, the terms of reference, or complete expert reports, unless the mock arbitration is focused on the particular issues for which these materials are relevant.
WHEN? Timing of the mock arbitration

When scheduling a mock arbitration, counsel should take care to conduct the exercise neither too early (that is, before the written record sufficiently articulates the terms of the debate) nor too late (so close to the real hearing date that counsel does not have enough time to absorb the lessons of the mock arbitration). Within those limits, counsel have two principal options for the timing of a mock arbitration: before the completion of pre-hearing briefing, or after. Each option has advantages and disadvantages.

In an “early” mock exercise, the major advantage is the ability to incorporate the mock arbitrators’ feedback into the next round of briefing – a significant benefit given the importance of written submissions in international arbitration. On the down side, an early mock arbitration is conducted on an incomplete record and subsequent written submissions can possibly give rise to new issues (or place greater focus on old issues) that the “early” mock arbitration left untested.

Even when no new issues arise in subsequent briefing, the mock arbitrators may discount some evidence and arguments, recognising that the record is incomplete and assuming that future submissions will contain counter arguments that muddy the waters.

In a “late” mock arbitration, the main advantage lies in the focus on preparing for the hearing. But this advantage comes at the expense of a chance to incorporate the mock arbitrators’ insights into the briefs, and a stronger hearing performance may not matter if a party's written submissions fall short.

Ultimately, correct timing for a mock arbitration depends on the relative importance of the hearing versus the parties’ written submissions, and on the reasons for conducting the mock arbitration within the specific circumstances of the case (which are typically a mix of improving presentation and refining substantive arguments).

HOW? Incorporating the feedback from a mock arbitration

The end result of a mock arbitration is the feedback and advice of the mock arbitrators, which can be collected in the following ways:

- observation of mock tribunal's deliberations;
- group interview of the mock tribunal;
- individual interviews of the mock tribunal's members; and/or
- written questionnaires.

To maximize the value of the feedback, counsel should encourage transparency and candour among mock arbitrators. To that end, conducting oral interviews or observing deliberations (which tend to be more open and freewheeling) are generally more useful ways to solicit feedback than soliciting answers to written questionnaires (which tend to be more cautious and self-censoring). In addition, mock arbitrators should not know which party counsel actually represents.

While counsel should give the mock arbitrators the opportunity to share their reactions in whatever order they prefer, preparing questions in advance can help ensure comprehensive feedback. Counsel may develop two kinds of prepared questions: general questions, and questions that are specific to the particular issues and evidence in the case. Topics for general discussion include:

- The degree to which the mock arbitrators had made up their minds before the mock hearing;
- The relative impacts of the written submissions versus the oral advocacy;
- The equities and which party or witnesses come across as “the good guy;”
- The strongest (and weakest) issues and evidence for each party;
- Which issues remain open or undecided; and
- What it would take to change a mock arbitrator’s mind on a given issue.
Once the mock arbitrators have addressed these and other topics, counsel must incorporate their feedback into the case. The process begins diagnostically, by isolating the common or unanimous points of agreement among a diverse panel of arbitrators, and determining the reasons for their agreement.

Counsel should be careful not to over-learn the lessons of the mock exercise, and to resist the impulse to radically reframe the case based on the mock arbitrators’ reactions. Unexpectedly favourable reactions deserve particular caution – if the mock arbitrators believe that a minor backup argument is actually the best argument, or that a major vulnerability is a trifle, it is likely that the mock hearing simply did not convey the weaknesses of these points thoroughly. Counsel ignores those weaknesses at their peril.

Negative reactions, by contrast, deserve special attention. A negative reaction that is expected or unsurprising (for example, when the mock arbitrators disregard an objectively weak claim) should be viewed as an invitation for counsel to devote their energies to more fruitful areas of the case rather than waste time on longshot arguments.

As for a negative reaction that is unexpected – perhaps the most significant form of feedback a mock arbitration can provide – counsel must build into their case the antidote to that reaction. But such adjustments should remain measured pivots, not great leaps to fundamentally re-engineer the case.

**WHY? Strategic goals of a mock arbitration**

When considering the various options for organising a mock arbitration, parties should keep in mind the strategic goals they seek to achieve through the exercise.

A mock arbitration can serve two principal goals: improving the presentation, and developing substantive arguments. The relative importance of each goal varies depending on the case – for example, developing substantive points may have special importance when choosing between clashing case themes of relatively equal strength, simplifying themes in a highly technical case, or evaluating evidence that supports some themes but undermines others.

Although a party can pursue the goals of presentation and substance simultaneously, the degree to which a mock arbitration is likely to advance each goal depends on various factors, including the timing, content, and structure of the mock arbitration, and on the identities of the participating mock arbitrators. Some of these factors (such as the content and structure of the mock arbitration) serve the goals of presentation and substance complementarily. Others (such as timing) involve unavoidable trade-offs between presentation and substance.

A mock arbitration that takes place after the submission of all briefing facilitates the preparation of counsel’s advocacy while doing little to improve the substance of the arguments; by contrast, an earlier mock arbitration would be more helpful in developing points of substance but less valuable as a “dress rehearsal” for the real hearing.

The selection of mock arbitrators could involve similar trade-offs between modelling the real tribunal’s approach to substantive legal issues and modelling the personality and presence each real tribunal member is likely to bring into the hearing room.

For example, a mock arbitrator could be chosen to replicate the inquisitive style of a member of the real tribunal who is known to be an active questioner, or the mock tribunal could be constituted to reflect the gender or nationality balance of the real tribunal. Such selections would likely improve the verisimilitude of the mock arbitration, but may come at the expense of the selection of mock arbitrators whose thought processes more closely align with their counterparts on the real tribunal.

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