HARBOUR
LITIGATION FUNDING

The 2nd Annual Harbour Lecture

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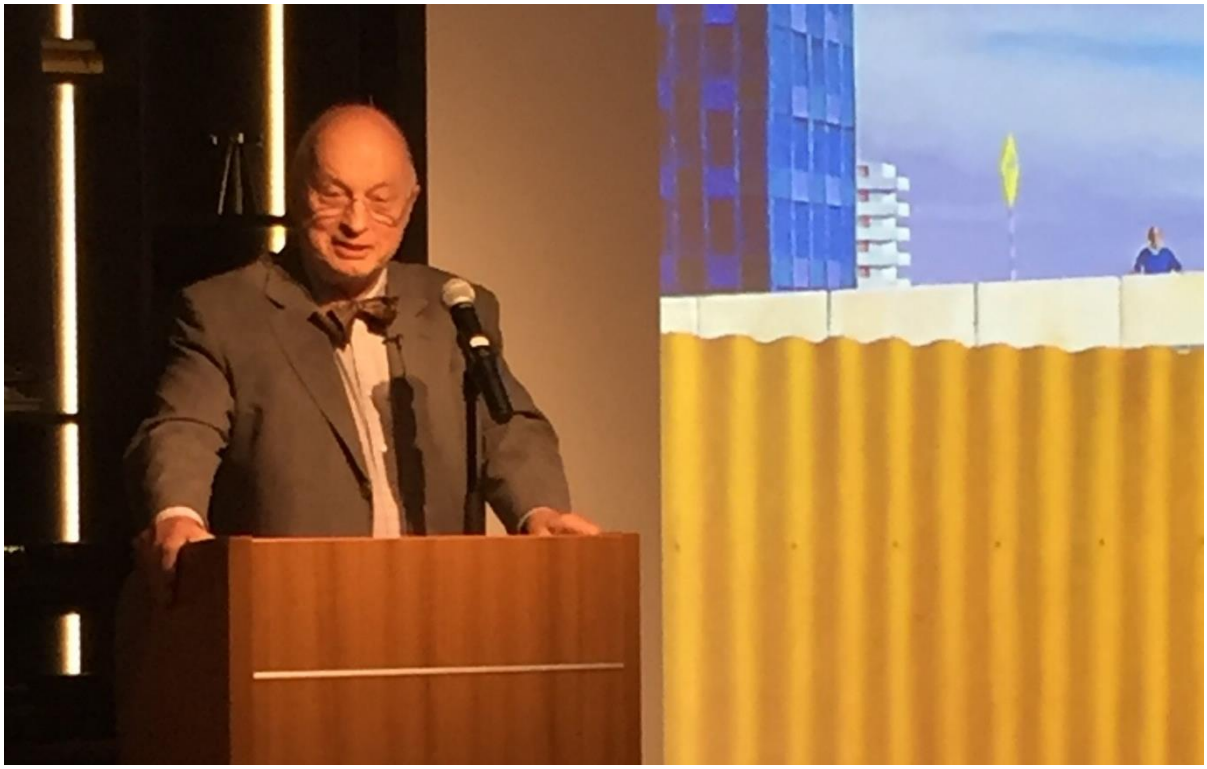
Mission accomplished or unfinished business? The rise and rise of litigation funding

***RSM v St Lucia* - 3 years on with 383.000 hits in 0.70 sec.**

Background notes for an extempore lecture.



Some of my best friends are litigation funders. I am delighted to have been invited by two of them, Susan Dunn and Ruth Stackpool-Moore to deliver the Second Hong Kong Harbour Lecture, following its 2016 launch by my arbitrator friend, Neil Kaplan, here present.

My first year Mercantile Law lecturer was an old silk who never made it to the High Court after sailing off to London in a slow boat sharing a posh First Class cabin with his secretary, and leaving behind his wife, the daughter of a Supreme Court Judge, and also his prospects for judicial appointment. I have retained one sentence from my first law class which has served me well -

> *Read all statutes to the end.*

Over 50 years this wise counsel has both won cases and kept me from losing them. My second take home point is even shorter -

I hot desk in chambers with Lord Millett who tells me why, as counsel, the present Lord Sumption was unplayable as an appeals advocate -

> He would open up: “My Lords, I will first deal with the strongest point against me. Having destroyed that he would submit: “Therefore I win”.

Strong and effective advocacy, which on delivery bowled over the learned Law Lords and left an unplayable wicket for opposing counsel.

> Precept 2: *Keep it simple: Less is more.*

I turn to explain the **image**: Geoffrey Smart died in Tuscany in 2013, aged 93, as the expatriate Australian artist loved for his depictions of Italian urban landscapes "full of private jokes and playful allusions". One of his most famous works is his "Portrait of Clive James", the London based Australian poet and slowly dying literary critic, barely to be identified behind the motorway's parapet.

The scene most aptly depicts my exposure at the parapet 3 years ago on publication *RSM v St Lucia*, an ICSID treaty case, where I flagged third-party funder costs issues as ripe for discussion (*see*, single page attachment).

My very brief declaration in 2014, in the context of investment disputes, was that costs issues arising from third party funders' engagement were much overlooked and were ripe for engagement and discussion.

Although it is now plain in retrospect that there was nothing radical or heretical in content, at least one surprised funder launched into rhetorical overreach to call me out as being all of –

> *Preposterous, intemperate, having mounted a soapbox, engaged in an absurd over the top diatribe, sadly lacking in judgment, and owing the arbitration community an apology.*

Three years, and some 363,000 hits in 0.70 seconds on, and with the issues I flagged now being addressed mainstream over 177 pages by the Draft ICCA/Queen Mary Task Force Report, I assure you that, unless one agrees with Oscar Wilde that "*the one thing worse than being talked about is not being talked about",* my position at the parapet immediately post-RSM was an uncomfortable and lonely place, captured as it was by GAR with images of "Pirates of the Caribbean" and "Alice in Wonderland". It sure sorts out your friends.

This presentation has two parts -

1 To declare ***Mission Accomplished*** for the third-party funding industry, in the George Bush sense of "almost" with some mopping up to attend to.

2 To hit the refresh button for security for costs issues, which I modestly claim to have enlivened from its long-standing moribund neglect in the fields of arbitration in general, and as it may affect third-party funders, in particular.

As to 1, I am residually anxious as I stroke funders' quite large egos by declaring that, as at October 2017, litigation funders have attained full maturity upon their admission as full members within the club of serious players in the disputes industry, judicial and arbitral, national and international.

There will be no Groucho Marx defence here:

> *I would not want to be a member of a club that would have me as a member.*

Undoubtedly, since 2014 third-party funders have moved to within the tent, bound by and contributing to emerging rules based regulation.

As I left law Office at the end of 1987, I was briefed in funded class action claims in State and Federal courts. Australian laws and practice had seen off old twins of champerty and maintenance, and a suite of legislative and regulatory procedural laws had blaized a trail formally to establish a flourishing environment for litigation funders.

Twenty years on the rest of the world has caught up. I entirely agree with Sir Rupert Jackson's recent laying of hands in judicial blessing on the admission of funders into the establishment tent -

> "*Litigation funding is beneficial, promotes justice, and should be supported."*

To this end, the industry is now populated with increasing numbers of agile and innovative entrepreneurs, spreading beyond one-off "plain vanilla" funding of claimants.

> *An aside: Tony Blair denies that George Bush Jnr said: "It is a pity the French do not have a word for entrepreneur".)*

The engagement with the funding industry over costs issues which I flagged in 2014 has become almost *the* big issue in international arbitrations. It is not merely 363,000 Google hits. The Draft **ICCA/Queen Mary Task Force on Third Party Funding in International Arbitration Report** issued 1 September 2017 over 177 pages has engaged the participation of 50 of the great and the good, as work in progress grappling with structural and procedural issues of current moment.

Redfern & O'Leary in their seminal recent piece in (2016) 32 *Arbitration International* 396, recast my limited observations limited to treaty disputes through to the recalibration of security for costs orders in commercial arbitrations generally, by proposing that they are a "highly effective weapon in the armoury of a defence lawyer to be employed without hesitation" (at 412). And, most recently, Christine Sim has engaged in a 67 page *tour d'horizon* of Security for Costs Issues in Investor State Arbitration in (2017) 32 Arbitrator International, 427 which exhaustively reprises the current state of debate.

During the same period, the reach of disputes funding has moved past the one-off funding to which I referred in RSM. Indeed, the business models of some larger funders have spread to financing rolling disputes of large and small players with arrangements directed to obtain the dual advantages of pricing out risk and taking uncertain liabilities off balance sheet.

And now, at the end of 2017, some principal litigators and legal services providers commonly enter arrangements with funders to manage and accelerate their cash flow by factoring off assets represented by work in progress, I am told sometimes to amounts beyond $100 m. The business model has recalibrated within some funders: one reports that nowadays less than 20% of its funding is committed to one-off disputes. Others more limit their books to "traditional" one-off disputes arrangements.

Even if the details of solutions remain work in progress, the Task Force Report confirms that the immediate alarm and concern, real or imagined, which so excited the industry after RSM, fairly may now be regarded as spent, or at the least worked around to an acceptable commercial result.

Within these variable arrangements, a convenient working definition of third-party, or litigation, funding is elusive. My preference for a workable content is adapted from the 60 year old, and somewhat physiologically based, test for obscenity of Justice Stewart Potter in the United States Supreme Court, in *Jacobellis v. Ohio* (1964) -

> *I know it when I see it*.

Funders *cf.* public interest litigators

Poverty of a plaintiff or claimant remains a handicap, not a privilege.

However, some funders press their altruistic credentials too far in proclaiming the benevolent reach of their operations. The reality is that there nothing much *pro bono publico* in the business models. As a class, funders are as tough as old boots, and engage in filtering processes directed to select only winners, through layers of due diligence, in-house and retained lawyers, accountants and damages experts and advisory boards.

The funders retain control of access to their funding much as bouncers do at a night club. My impression is that, as a group, funders are excessively cautious and risk adverse. The process of review is deep and defensive. No "justice" based filter there.

The Draft Task Force Report, at 160, suggests that only 1 in 10 applications to these "*new venture capitalists*" is accepted. To adapt what Rupert Murdoch's self description in another context over 40 years ago after he turned the failed London Sun newspaper around to profitability, funders run on "*the smell of success".*

Of course, wrong calls are made: ICSID statistics confirm many investment claims fail, and the average recoveries for the successful are a fraction of amounts claimed. The unknown known is the proportion of failed funded claims. I suspect fairly low.

Costs insurance

As I understand it, once it became apparent post RSM that there was a previously unperceived risk for security for costs orders becoming made *en passant* during the course of disputes, as of course provisions for such costs became included in budgets at inception and insurance protection extended to cost out risks.

To this extent, even entire risk of losses arising from a dismissed claim, including adverse costs orders, may be converted, at a substantial price, from being an uncertainty to being an input in overall case management. Through such arrangements some funders' business plans may more be seen to have migrated into "partnerships" with other financial players including insurers and other financial entities.

It sounds a little like "*Heads I win: Tails I do not lose"* which leads me to the "hot" issue, enlivened by *RSM*, concerning security for costs orders in international arbitrations, both generally and also as they may affect third party funders in particular.

Security for Costs Orders

It is trite that -

1) In common law systems with costs jurisdictions the courts have direct powers to make security for costs orders against both parties and non-parties, including funders;

2) Arbitrators in domestic and international arbitrations are not enabled to direct costs orders against non-parties.

As to 2), in international commercial disputes tribunal's costs powers are derived from the law governing the arbitration and from the consent of the parties, most commonly arising from their agreement as to the law of the seat and the particular set of institutional rules that apply.

Apart from some residual but resolving controversy as to the position under the UNCITRAL Rules, the institutional Rules have come almost universally to provide authority for tribunals to make security for costs orders, including ICC, LCIA, HKIAC, SIAC, KLRCA, ACICA etc. This coverage is conveniently summarised by Redfern & O'Leary, 403 to 412.

However, until 2014 (dare I say RSM?) and notwithstanding their ample statutory and rule based powers to do so, there were little or no jurisprudence and few examples of security for costs orders being made against claimants by tribunals in national and international arbitrations.

For example, in the *Ken-Ran Case* [1994] 2 All ER 449-478, where a majority the English Court of Appeal exceptionally confirmed a tribunal's securities for costs order, Lord Mustill dissented on the ground that in international arbitrations such orders "are not the done thing". As recently as 2000, Craig, Park and Paulsson, agreed that they were "inappropriate". And through to the last few years, gentlemen eschewed applications for such orders and they were rarely sought: See generally *Redfern & O'Leary (2016) 32 Arbitration International, 399-400. ("Gentlemen" are not a gender neutral concept: One working definition as I came to the Bar was that a gentlemen's agreement is not worth the paper it is not written on. The noun appears incapable of a gender-neutral rendition*)

Redfern & O'Leary, 403 - 412 continue on, to make a powerful case to reverse the gentlemen's inertia against such orders being made all in international arbitrations to characterise them as a "highly effective weapon in the armoury of a defence lawyer to be employed without hesitation".

[*I recommend the entire Redfern and O'Leary, piece as a powerful recalibration of the position of security for costs orders in international commercial arbitration*.]

In summary, by predisposition or neglect, and despite ample powers, through August 2014 there was virtually no international practice in international arbitrations even to seek security for costs orders against claimant perceived as not good to meet adverse costs awards.

For this reason, pre-RSM, the live possibility of exposure to security for costs orders in international commercial or investment arbitrations appears never to have come within the range of the funders' cost avoiding radar. Much like the guns at Singapore: the funders were facing the wrong way.

Hence, because of the absence of costs practices in international commercial disputes generally it was left to the majority in RSM to fire the starting gun as to issues relevant to security for costs orders affected by issues of litigation funding.

There were 2 steps –

First, did the power to order security for costs arise under the terms of the ICSID Convention?

RSM was a majority decision, with Dr Elsing and myself, finding that there was such a power. In doing so we confirmed the prevailing writings on the issue. Judge Nottingham, a former US Federal Court Circuit Judge wrote in strong dissent, with persuasive contrary arguments. As Wellington said after Waterloo: "*It was a close run thing*" and could have gone either way. Maybe it will, as the RSM's application for Annulment remains in the lists.

Second, the exercise of the power

The majority in RSM qualified our recognition of a capacity to make security for costs orders as embedded in the Convention by expressing the principle as confined in its exercise to truly exceptional circumstances, with the two of us agreeing that the fact of third party funding was a relevant consideration.

The enduring controversy arose from me going beyond the particular facts concerning the Claimant's claims history, with short assenting remarks (as attached to this paper) commenting that the decision to find power under the Convention flagged as ripe for discussion the relevance, if any, of a third party funder's participation in a treaty dispute where applications for security arise *and* the claimant is established as unable to meet adverse costs orders.

I flagged 3 brief propositions as relevant for discussion -

Proposition 1: In contrast with litigation and commercial arbitrations, save in exceptional circumstances, security for costs should not be made in an investment dispute against an insolvent claimant, funded or not funded.[1]

Proposition 2: Where a funded claimant is not established as being unable to meet adverse costs orders the fact of third party funding is irrelevant, and security for costs order should not be made.[2]

Proposition 3: Where a funded claimant is established as unlikely to meet an adverse cost order, on an application by a State respondent, and as a discretionary matter, consideration may be given to make security for costs orders against the claimant.[3]

Within the specialist field of investment disputes, RSM found that only most exceptionally should security for costs orders be made against an insolvent Claimant however plain it was that final adverse costs would not be met. The position is *contra* in commercial arbitrations.

My position, was and remains, is that notwithstanding the excitement and alarm generated by funders upon the publication of RSM, these 3 propositions may now be seen to self-evidently relevant when made, as now indicated by their continuing engagement in consideration as by the ICCA/Queen Mary Task Force in the broader fields of commercial (cf treaty) arbitrations.

In summary, and to put the post-RSM controversy in context, RSM identified two "hot" issues:

First, as an unintended backfill, the decision reached back and opened up the security for costs issues in international commercial arbitration from where it had been quietly hidden in the long grass by the gentlemen players.

RSM does not address that issue. Redfern and O'Leary have since identified and run with that. Their September 2016 piece is a must-read game changing review of the state of play over security for costs issues quite apart from funder issues.

Second is the confirmed acceptance of the relevance of a third party funder standing behind a claimant in arbitrations, where, cf. litigation, direct orders for costs cannot be made against third parties.

[1] Paragraphs 2 and 3.
[2] Paragraphs 2, 3 and 16 (last sentence).
[3] Paragraphs 10 to 14 and 16.

What was hot became hotter with the publication of the Draft Task Force Report on 1 September 2017 compiled and issued by the more than 50 of the great and the good in international arbitration.

Each page is headed "Do not Cite", but I ask what else are we meant to do with it?

Chapter 8 concerns third party funding in Investment Disputes (the RSM situation), with only the last 6 pages of the entire 177 engaging in a somewhat too neutral examination of the securities for costs funding issues.

Usefully, at 167, the Draft Report states that the prevailing State view is that it is unfair if an adverse costs order cannot be recovered from an impecunious claimant or reimbursed by a third-party funder sharing the prospect of gain.

The heads I win issue issue from RSM.

And more interestingly, given the dismay expressed by some funders as RSM was published, at 168, it is stated that some funders nowadays are agnostic about security for costs orders because they may be added for recovery under the funding agreement.

That confirms my comment that the funders' caravan has moved on and that, in general, funders have sorted their risks and costs allocations to cost-in the possibility that security for costs order may be made in both funded commercial and investment disputes.

Indeed, as the Task Force confirms, for funders the risk of financial exposure that caused so much excitement when RSM was published now is close to a dead issue. The Draft Report identifies the general principles for the conflicts disclosures are more important to both parties and funders than the security for costs aspect which so exercised them as RSM was published at end 2014.

Onus

In RSM, I made passing reference to the issue of proof of financial incapacity once the issue was raised in the context of a treaty claim.

Chapter 6 of the Draft Report is directed to recommendations on that general issue of security for costs where there is a funding arrangement, to enable relevant disclosure by the funded claimant of its funding and financial circumstances once the issue of security for costs is raised.

On the security for costs orders issue, the recommendations in Chapter 6, concerning onus, read as unworkable. Indeed, Recommendation 2, at 114, is Rumsfeldian in requiring a moving party first to establish a *prima facie* case showing impecuniousness before the other party need defend its financial state.

Inasmuch as Alice was brought into this issue by GAR's initial write up of RSM, the proposal appears to reflect the Victorian authority of *R. v Lewis Carroll; ex. P The Queen of Hearts* in its logical perversity: first the verdict and then the trial. It is only a recommendation and presents, as do other parts of the Draft Report, merely as a first bid compromise as work in progress.

In RSM, I observed the moving party does not have access to the claimant's financial position, especially in investment disputes. For the moment the balance of debate appears to be

struggling to find sensible traction on the onus issue by proposing initial proofs of insolvency from the party raising the challenge.

RSM Issues

Maybe in RSM I should not have signposted the obvious issues that appeared to arise from the RSM decision. And with hindsight, I admit should have been less adjectival in my brief identification of those issues. I did not realise how insecure and touchy were some CEOs of this fledgling industry.

My reference to "mercantile adventurers" was intended to embrace the image of a disruptive new business entity: the "Uber" of arbitration funding. No element of implied denigration or offence may be gleaned from the OED definitions of "adventurer" nor was that intended. The Task Force Report omitted the "*ad*" in applying the description "*commercial venturers*" to convey the same meaning. Maybe if I also had left off the "ad" GAR would not have conjured up the image of "Pirates of the Caribbean".

Maybe also, I should not have further excited funders by describing their position outside the tent as an equivalent "*Gambler's Nirvana: heads I win and tails I do not lose*". The description was colourful, but, as is noted by the Task Force (at 177), is accurate as a fair summary of the "no loss" odds.

Be that as it may, 3 years on, the funders now are established inside the tent, firmly engaged with the stakeholders both taking benefits and subject to obligations within the development of formal processes of regulation directed to derive workable solutions to complicated issues.

October 2017 is not August 2014.

Lord Denning, who called me to the English Bar at Lincoln's Inn 49 years ago, once dismissed the floodgates argument in terms -

> "*Open the floodgates and the trickle comes through*".

There have been few, but an increasing number, of applications for security for costs against unfunded and funded claimants both in commercial and in treaty disputes. On this issue of security for costs issues the report is work in progress.

The issues enlivened in RSM remain alive, and in a wider context than treaty disputes. They were nascent at the time of RSM, whether or not I had flagged them. It is now accepted that in commercial investment disputes, the fact of funding is a relevant consideration on applications for security for costs, with some continuing uncertainty as to the procedural consequences.

RSM v St Lucia: 14 August 2014 –

Gavan Griffith QC - Assenting observations directed to security of costs and litigation funders

2. *In a real sense, the risk to a State of a self-identifying investor claimant under a BIT having no funds to meet costs orders is inherent in BIT regimes. As a general proposition it may be said that a State party to a BIT has prospectively agreed to take claimant foreign investors as it finds them. That the claimant does not have funds to meet costs orders if unsuccessful is no reason to make orders for security. Commonly, this situation is contended to arise from the matters of complaint, and it would be inconsistent with the BIT entitlements for such financial issues arising from its lack of funds to derogate from the investor's treaty entitlements.*

3. *It follows, that save in truly exceptional circumstances there is little scope for security for costs orders being made against a claimant simpliciter under a BIT claim.*

10. *It is increasingly common for BIT claims to be financed by an identified, or (as here) unidentified third party funder, either related to the nominal claimant or one that engages in the business venture of advancing money to fund the Claimant's claim, essentially as a joint-venture to share the rewards of success but, if security for costs orders are not made, to risk no more than its spent costs in the event of failure.*

11. *Such a business plan for a related or professional funder is to embrace the gambler's Nirvana: Heads I win, and Tails I do not lose.*

12. *The founders of the Convention could not have foreseen in any way the emergence of a new industry of mercantile adventurers as professional BIT claims funders. It is no reach to find that, as strangers to the BIT entitlement, such funders also should remain at the same real risk level for costs as the nominal claimant. In this regard, the integrity of the BIT regimes is apt to be recalibrated in the case of a third party funder, related or un- related, to mandate that its real exposure to costs orders which may go one way to it on success should flow the other direction on failure.*

13. *Costs orders may be significant, the more so proportionally to a small State such as the Respondent here. An extreme recent example of costs awards in a Treaty claim is the recent Award in Hulley Enterprises Ltd (Cyprus) v The Russian Federation (18 July 2014), where the claimant's costs were allowed at $79 m.*

14. *For these brief reasons, my position is that, unless there are particular reasons militating to the contrary, exceptional circumstances may be found to justify security of costs orders arising under BIT claims as against a third party funder, related or unrelated, which does not proffer adequate security for adverse cost orders. An example of contrary circumstances might be to establish that the funded claimant has independent capacity to meet costs orders.*

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