CHAPTER 10

Article 38 of the SCC Rules: An Analysis of Security for Costs in TPF Arbitration

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§10.01 THE RAPID DEVELOPMENT OF THE FUNDING MARKET

As a means for businesses to finance legal claims, Third-Party Funding (TPF) has become an increasingly important procedural feature of international arbitration.[1] The market is constantly growing and involves a variety of actors, as well as substantial assets.[2] In Sweden (as of today), a viable internal TPF market does not seem to exist.[3] There are no formalized legal or self-regulatory regimes regulating TPF and its impact on the arbitral procedure in Sweden. Despite this, TPF is of significant importance in the Swedish context. Sweden is commonly chosen as arbitral seat, and the Stockholm Chamber of Commerce (SCC) oversees international arbitrations on a continuous basis. Consequently, a noteworthy amount of international arbitrations involving TPF are seated in Sweden.[4] While the reception of TPF was previously hostile and even in some respects fiercely sceptical, the contrary standpoint is now cementing itself as commonplace. The reasoning by the tribunal in *Giovanni v. The Argentine Republic* illustrates the pro-TPF wave in international arbitration. It reasoned that: '[TPF] is by

1. *See*, e.g., Jonas von Goeler, *Third-Party Funding in International Arbitration and Its Impact on Procedure* 1–8 (2016), Lisa Bench Nieuwveld and Victoria Shannon Sahani, *Third-Party Funding in International Arbitration* 1 (2nd ed. 2017), and Marie Stoyanov and Olga Owczarek, *Third-Party Funding in International Arbitration: Is It Time for Some Soft Rules?*, 2 BCDR Int'l Arb. Rev. 171, 171–172 (2015).
2. *See* Jonas von Goeler, *supra* n. 1 at 75–76.
3. Johan Sidklev & Carl Persson, *Sweden*, Ch. 15, in *The Third Party Litigation Funding Law Review* 145 (1st ed. 2017).
4. Johan Sidklev & Carl Persson, *supra* n. 3 at 145. *See also* Johan Sidklev et al., *Third Party Funding – Uncovering Uncharted Territory*, Kluwer Arbitration Blog (16 Sept. 2018).

now so well established both within many national jurisdictions and within international investment arbitration that it offers no grounds in itself for objection.'[5]

This notwithstanding, TPF does, indeed, trigger a number of legal concerns relating to how the involvement of third-party funders affects arbitral procedure.[6] One of the more pressing issues relates to the difficulties for the non-funded party to obtain reimbursement for costs.

§10.02 'THE RESPONDENT'S DILEMMA'

A party taking recourse to TPF often – however not necessarily always – operates out of a precarious financial situation.[7] An impecunious party may lack assets that could be attached in the event of an adverse judgment. Consequently, good faith concerns arise as to the consequences of the funded party losing the arbitration. Prior to deciding whether or not to fund a claim, the funder conducts a cost-benefit analysis focused primarily on the merits of the case (including extensive jurisdictional inquiries in investment arbitration) and the enforceability of the award.[8] The prevalent goal of this 'calculus' is to analyse the probability of a successful outcome against three main concerns. Those are: (1) the strength of the claim as to merits of the case; (2) the likelihood that an award will be enforced and the costs for such enforcement measures; and (3) the value of the potential outcome of the case (*quantum*).[9] Generally, the funding calculus is scrupulous and funders are reluctant to fund cases if the probability of success is not considerable.[10] Yet, a claim may often prove to be weaker than anticipated due to, for example, unexpected revelations made during discovery. Thus, notwithstanding a thorough pre-case analysis, accurately predicting the outcome of an arbitration before its initiation is – if not impossible – very difficult.[11] As a result, there is always a non-negligible likelihood that a funded claim is unsuccessful. Should the funded claimant lose the arbitration, the funder's risk materializes and the investment turns fruitless.[12] Concurrently, the winning party faces the challenge of enforcing an arbitral award against an impecunious counterparty. This will of course be problematic, if the funded party lacks attachable assets.

Arguably, these predicaments of the non-funded party reflect the very nature of arbitration, *viz.* that winning on the merits entails no guarantee of successfully enforcing the award. Moreover, TPF does serve the (desirable) purpose of providing access to justice for parties that would otherwise be unable to bring a claim to

5. ICSID Case No. ARB/07/8, Decision on Jurisdiction and Admissibility, 128 (17 Nov. 2014).
6. *See*, e.g., Report for public discussion of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration, Apr. 2018. The ICCA Reports No. 4.
7. Jonas von Goeler, *supra* n. 1 at 82.
8. *Id.* at 92.
9. *Id.* at 14–15.
10. *Id.* at. 25.
11. Selvyn Seidel, *Third-Party Investing in International Arbitration Claims to Invest or Not to Invest? A Daunting Question*, Ch. 10 in *10 Third-Party Funding in International Arbitration (ICC Dossier)* 16 (Bernardo M. Cremades Sanz-Pastor & Antonias Dimolitsa eds. 2013).
12. Stephen Jagusch, *Third Party Funding of International Arbitrations* Ch. 8 in *The Leading Arbitrators' Guide to International Arbitration* 209 (3rd ed. 2014).

arbitration.[13] Nonetheless, the difficulty of securing payment from an impecunious counterparty entails that a winning party may end up bearing the risk for the accuracy of the funder's pre-investment predictions.

This chapter addresses some of the means accessible for a party to vindicate its rights and secure its position when faced with third-party funded claims brought by impecunious adversaries in international arbitrations seated in Sweden. The analysis focuses on how the non-funded party may secure legal fees by utilizing the mechanism of security for costs. In 2017, a new provision expressly introducing security for costs as an available provisional relief was included in the SCC Rules. This provision (Article 38) is unique in a Swedish setting and will constitute the main point of reference throughout this chapter. However, as will be revealed further below, the lack of guiding SCC case law creates uncertainty as to how the provision should be applied in practice, not the least in relation to cases involving TPF. The crux confronted by a seized tribunal assessing security for costs is twofold: (1) how the claimant's state of impecuniosity; and (2) the presence of a third-party funder relate to the general standards for granting security for costs in international arbitration practice. A further crucial question is whether – for the purposes of properly assessing the standards for granting security for costs – an arbitral tribunal may order a party with TPF to: (a) disclose the source of the funding; and (b) the terms and conditions behind the funding agreement.

§10.03 SECURITY FOR COSTS IN SWEDEN: A DISTINCTIVE FORM OF PROVISIONAL RELIEF

As of today, most arbitration laws and rules allow for interim measures in order to, among other things, preserve assets or to order a party to take – or refrain from taking – a certain action.[14] Section 25(4) of the Swedish Arbitration Act (SAA) reads as follows: '[u]nless the parties agreed otherwise, the arbitrators may, at the request of a party, decide that, during the proceedings, the other party must undertake a certain interim measure to secure the claim, which is to be tried by the tribunal'. Provisions in arbitration rules often leave a wide discretion to the tribunal to assess the need for interim measures.[15] However, the assessment of the tribunal usually aims to establish whether the moving party has prima facie shown: (1) a likelihood of success with regards to the merits of the claim(s) or counterclaim(s); (2) an irreparable harm; (3) urgency; and (4) proportionality.[16]

Security for costs as a provisional relief should, however, be distinguished from what the SAA refers to as 'interim measures'. The concept of security for costs is originally a common law phenomenon which has rarely been used in arbitrations and

13. Christopher P. Bogart, *Overview of Arbitration Finance*, Ch. 4 in *10 Third-Party Funding in International Arbitration (ICC Dossier)* 50 (Bernardo M. Cremades Sanz-Pastor & Antonias Dimolitsa eds. 2013).
14. Cf. Nigel Blackaby et al., *Redfern & Hunter on International Arbitration* 317–318 (6th ed. 2015).
15. Gary Born, *International Commercial Arbitration* 2467 (2nd ed. 2014).
16. *Id.* at 2468.

litigations taking place in jurisdictions of civil law tradition. However, as pointed out by Gary Born, '[s]ecurity for costs is a common form of interim relief in arbitrations with their seat in England or Commonwealth jurisdictions, where this type of relief is a routine aspect of domestic litigation'.[17] Notable examples of institutional arbitration rules that include provisions on security for costs – which all originate out of a common law oriented approach – include, *inter alia*, the LCIA Arbitration Rules (2014), the Arbitration Rules of the Singapore International Arbitration Centre (SIAC) (2016), and the Hong Kong International Arbitration Center (HKIAC) Arbitration Rules (2018).[18] While security for costs has previously been treated with scepticism by arbitrators with civil law background, a shift in attitude seems to have taken place during the course of recent years. As further stated by Born:

> Historically, tribunals without English or Commonwealth orientations were skeptical of both their authority to order security for costs and of the wisdom of doing so (sometimes on the basis that security for costs may deprive a party with limited financial means of the opportunity to pursue its claim). More recently, however, many international tribunals have been willing, at least in principle, to consider requests for security for costs [citations omitted].[19]

In Sweden, provisional relief as a mechanism for securing legal costs has traditionally not been used either in domestic litigation nor arbitration proceedings. Thus, although security for costs is not a new feature of arbitral procedure in general, it can be considered as a novelty in a Swedish context. This is evident not the least by the fact that the primary function of section 25(4) of the SAA is to enable security for the claimant's underlying substantive claim and not the legal costs estimated to be induced as a result of pursuing such a claim.[20] Furthermore, security for costs orders differ from 'ordinary' interim orders in that they are issued under the imminent threat of a stay of the proceedings or dismissal of the claimant's claim, which diminishes the importance and utility of state assistance as an element of enforcement.[21] In light of this, the mechanism of security for costs arguably does not constitute an 'interim measure' as defined under the SAA. This also entails uncertainty as to whether security for costs is available in ad hoc arbitrations seated in Sweden.

[A] Security for Costs under the SCC Rules

[1] Article 38: Introducing Security for Costs in Sweden

The broad power of the tribunal set out in the SAA to issue interim measures is reflected in Article 37(1) of the SCC Rules, which allows for 'any interim measures [the tribunal]

17. *Id*. at 2495.
18. *Id*.
19. *Id*.
20. Cf. Born, *supra* n. 15 at 2495 where Born highlights the English Arbitration Act, 1996, as an example of arbitration legislation that includes a specific provision on security for costs.
21. Weixia Gu, *Security for Costs in International Commercial Arbitration*, 22 J. Int'l Arb. 167, 167 (2005).

deems appropriate'. However, as noted above, it is questionable whether security for costs at all constitutes an 'interim measure' according to the SAA. Furthermore, prior to the most recent revision of the SCC Rules in 2017, in part, because the issue had not previously been subject to any extensive doctrinal discussions,[22] it was deemed uncertain whether or not the SCC Rules encompassed the authority for the tribunal to order security for costs. Consequently, to elucidate that security for costs is an available feature of SCC proceedings, the SCC deemed that an entirely new provision was required. Accordingly, the SCC Rules now include a provision specifically on security for costs. Article 38(1) of the SCC Rules states that '[t]he Arbitral Tribunal may, in *exceptional circumstances* (emphasis added) and at the request of a party, order any Claimant … to provide security for costs in any manner the Arbitral Tribunal deems appropriate'.

Generally, in international arbitration practice, there is no uniform approach as regards the appropriate standard for when an order for security for costs is justified.[23] However, case law, notably from the International Chamber of Commerce (ICC), indicate that the choice of the wording 'exceptional circumstances' in the SCC Rules was not coincidental.[24] In a special supplement issued by the ICC in 2014 on procedural decisions, it is stated that '[the tribunal's] power to order conservatory measures … is generally thought to include the power to order security for costs. However, this is a power used rarely and restrictively'.[25] In other words, it seems as though the restrictiveness suggested by the wording of the Article 38 of the SCC Rules, stems from an internationally recognized view that security for costs should, as a rule, not be granted unless there are special reasons for doing so.[26]

As for the specific criteria for granting security for costs, Article 38(2) of the SCC Rules provides that:

> In determining whether to order security for costs, the Arbitral Tribunal shall have regard to: (i) the prospects of success of the claims, counterclaims and defences; (ii) the Claimant's or Counterclaimant's ability to comply with an adverse costs

22. However, *see*, e.g., Robin Oldenstam & Johann von Pachelbel, *Practitioner's Handbook on International Commercial Arbitration*, 11.161 (2009). Therein, the authors comment on the equivalent provision (Article 32) in the 2007 Rules (which remained unchanged after the revision in 2010) stating that '[t]he arbitrators cannot, however, order a party to provide security for the other party's costs in connection with the proceedings [citations omitted]'.
23. Weixia Gu, *supra* n. 21 at 186.
24. *See*, e.g., *X v. Y and Z*, ICC Case, Procedural Order of 3 August 2012, para. 24 where the tribunal stated that security for costs should 'not be granted easily', and ICC Case No. 10032 Order dated 9 Nov. 1999 in which the tribunal labeled security for costs as an 'exceptional measure'.
25. *See* Special Supplement 2014: Procedural Decisions in ICC arbitration. The supplement contains nine procedural orders issued by ICC tribunals on security for costs. In six of these cases, security for costs was rejected by the tribunal. As for the three remaining cases (in which security for costs was granted in part or subject to conditions), the supplement states that '[e]xceptional circumstances that were considered to justify ordering security for costs included a degree of impecuniousness beyond mere insolvency or financial weakness, a change of circumstances so severe as to jeopardize the enforceability of a future award of costs, and the deliberate alienation of funds to avoid liability'.
26. Cf. Report for public discussion of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration, Apr. 2018. The ICCA Reports No. 4, at 166.

> award and the availability of assets for enforcement of an adverse costs award; (iii) whether it is appropriate in all the circumstances of the case to order one party to provide security; and (iv) any other relevant circumstances.

An explicit condition is the existence of a claim and its outlooks for success. However, the influence of a third-party funder and the claimant's financial situation are not circumstances that affect the existence or strength of a claim.[27] Instead, the claimant's impecuniousness and the existence of a third-party funder bear weight in relation to the requirements laid out in Article 38(ii) of the SCC Rules, i.e., 'the Claimant's … ability to comply with an adverse costs award and the availability of assets for enforcement of an adverse costs award'.

An impecunious claimant may be without attachable assets and presumably has a limited ability to comply with an adverse costs award. Consequently, at a first glance, Article 38(ii) might be interpreted as suggesting that the respondent has good chances for obtaining security for costs merely based on the claimant' impecuniousness in conjunction with TPF involvement. Nonetheless, as noted above, the wording 'exceptional circumstances' in Article 38 of the SCC Rules indicates significant restrictiveness.

[2] International Outlook: Security for Costs in Relation to TPF

As noted above, international practice suggests that a tribunal should not grant security for costs unless there are strong and convincing arguments for doing so. Moreover, Article 38 of the SCC Rules clearly indicates that the claimant's ability to bear adverse costs is clearly an important factor in the tribunal's assessment. However, the influence of the existence of a third-party funder on the assessment is not as clear. In light of this, the mere wording of the Article 38 does not provide sufficient basis for analysing the prospect of a party to receive security for costs in an SCC arbitration brought by a funded and impecunious adversary.

Moreover, as of yet, there is no SCC practice providing guidance for resolving this issue.[28] However, there are numerous international arbitration cases adjudicated abroad that address security for costs in disputes involving TPF. The reasoning of the tribunals in these cases may be indicative of how an SCC tribunal seated in Sweden would treat similar situations. Moreover, when delving deeper into the specifics of TPF, the developed body of arbitration cases provides considerable guidance as to when such measures are warranted.

27. Laurent Lévy & Regis Bonnan, *Third-Party Funding Disclosure, Joinder and Impact on Arbitral Proceedings*, Ch. 7 in *10 Third-Party Funding in International Arbitration (ICC Dossier)* 79 (Bernardo M. Cremades Sanz-Pastor & Antonias Dimolitsa eds. 2013).
28. To the author's knowledge, as of November 2018, security for costs under Article 38 of the SCC Rules had been applied for on four occasions. In three of those instances, the tribunal rejected the request. The remaining request was withdrawn by the requesting party.

Guarachi v. Bolivia (2013)[29]

In *Guarachi v. Bolivia*, the respondent asserted the existence of the claimant's TPF in conjunction with an analysis of the claimant's balance sheet and other financial documents (allegedly showing impecuniousness) as the basis for a request for security for costs.[30] First, the tribunal concluded that the authority to grant security for costs derives from Article 26 of the UNCITRAL Arbitration Rules (as revised in 2010).[31] The tribunal also emphasized that an 'order for posting of security for costs remains a very rare and exceptional measure'.[32] Furthermore, the tribunal decided that the asserted circumstances were not sufficient for establishing that the claimant would be unable to comply with an adverse costs award and thus rejected the request.[33]

RSM v. Saint Lucia (2014)[34]

The majority decision in *RSM v. Saint Lucia* constitutes the first example of where an ICSID tribunal ordered security for costs based on the existence of TPF. In its reasoning, the tribunal initially underlined that '[a]s previously held by previous [ICSID] tribunals, [an order for security for costs] can only be made in exceptional cases [citations omitted]'.[35] The claimant in the case had shown reluctance to comply with previously rendered cost orders. On that basis, the tribunal stated that:

> [It] has been established to the satisfaction of the Tribunal that Claimant does not have sufficient financial resources. Whereas it has previously been held that such financial limitations as such do not provide a sufficient basis for ordering security for costs, the circumstances of the present case are different. In particular Claimant's consistent procedural history in other ICSID and non-ICSID proceedings provide compelling grounds for granting Respondent's request [citations omitted].[36]

As to the existence of third-party funding, the tribunal stated that 'the admitted third-party funding further supports the Tribunal's concern that claimant will not comply with a costs award rendered against it, since, in the absence of security or guarantees being offered, it is doubtful whether the third party will assume responsibility for honouring such an award'.[37] On those grounds, the tribunal granted the request for security for costs.[38]

Thus, the tribunal put significant emphasis on the claimant' procedural history of failing to comply with costs orders. Furthermore, it also viewed TPF as indicative of the

29. *Guaracachi America Inc. and Rurelec PLC v. The Plurinational State of Bolivia*, UNCITRAL, PCA Case No. 2011-17, Procedural Order No. 14 (11 Mar. 2013).
30. *Id.* para. 7.
31. *Id.* para. 5.
32. *Id.* para. 6.
33. *Id.* para. 7.
34. *RSM Corporation v. Saint Lucia*, ICSID Case No. ARB/12/10.
35. *Ibid.*, Decision on Saint Lucia's Request for Security for Costs with Assenting and Dissenting Reasons, para. 75 (13 Aug. 2014).
36. *Id.* para. 82.
37. *Id.* para. 83.
38. *Id.* para. 90.

claimant's ability to comply with an adverse costs award. The underlying reasoning, moreover, embraces the perception that third-party funders do not commit to cover any other costs than those incurred directly by the funded party.[39]

The position held by the majority in *RSM v. Saint Lucia* gave rise to heated controversy. In a dissenting opinion, Edward Nottingham, argued that: '[i]n reaching its decision concerning security for costs, the Majority relies in part on its conclusion, based on the sketchiest of records, that Claimant has third party funding to finance its case'.[40] He further accentuated that neither the ICSID Convention nor Rules are properly equipped to handle any alleged problems associated with TPF. He argued that: '[u]ntil the Administrative Council is more explicit about the matter, an individual tribunal should not be using general language of unlimited elasticity to accomplish the result which the tribunal regards as appropriate'.[41] Nottingham's position highlights the absence of clear rules vis-à-vis the complexities relating to the issuance of security for costs and disclosure orders in funded arbitrations.[42]

Gavan Griffith, on the other hand, in an assenting opinion, expressed fierce criticism towards TPF's inferences on arbitral procedure. He argued for a generous view on ordering security for costs and stated that, unless such orders are issued, '[s]uch 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'.[43] Griffith's statements viewing the funding business as a gambler's 'Nirvana' were in turn criticized by Christoph Bogart who, in addition to expressing support for Edward Nottingham's viewpoint, wrote that:

> Of course, that's not just wrong, but absurd. To begin with: Tails, we do lose, and very much so. Firms like Burford put up millions of dollars to assist claimants with their financing needs in bringing an arbitration claim. If the claim does not produce a recovery, the funder will typically lose all of its invested capital. That is a powerful incentive to do extensive diligence and to screen out frivolous and spurious claims.[44]

Eurogas v. Slovak Republic (2014)[45] and *South American Silver Ltd. (SAS) v. Bolivia* (2015)[46]

Subsequent to *RSM v. Saint Lucia*, the tribunals in *Eurogas v. Slovak Republic* and *SAS v. Bolivia* demonstrated a more restrictive approach vis-à-vis security for costs,

39. *Id.*
40. *Id.* Dissenting opinion of Edward Nottingham, para. 17.
41. *Id.* Dissenting opinion of Edward Nottingham, para. 20.
42. This is an issue of significant importance in investor-state arbitrations where imposing binding provisional measures without clear support the applicable treaty may interfere with state sovereignty. For a further discussion on this vis-à-vis provisional measure under the auspices of ICSID, *see* Ylli Dautaj & Bruno Gustafsson, 'The Binding Nature of Provisional 'Recommendations' in ICSID Arbitration' Kluwer Arbitration Blog (27 Jun. 2018).
43. *Supra* n. 35. Assenting reasons of Gavan Griffith, paras 12–13.
44. Christoph Bogart, *RSM v. St. Lucia: Why the majority got it wrong on security for costs* (9 Nov. 2014), http://www.burfordcapital.com/blog/rsm-v-st-lucia-majority-got-wrong-security-costs/).
45. *EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic*, ICSID Case No. ARB/14/14.
46. *South American Silver Limited v. Bolivia*, UNCITRAL, PCA Case No. 2013-15, Procedural Order No. 10 (11 Jan. 2016).

inter alia, by highlighting that TPF per se is not evidence of the claimant's impecuniousness.

The respondent in *EuroGas v. Slovak Republic* requested security for costs on the basis that the claimants '[were] not capable of satisfying a costs award and [had] a history of engaging in fraud and reneging on payment obligations'.[47] The respondent further argued that '[the claimants] do not have the means to pay for the costs of the arbitration proceedings, which are entirely funded by third parties'.[48] The tribunal addressed the reasoning in *RSM v. Saint Lucia*, which was relied upon by the respondent, and denied the request on the following basis:

> It is true that in RSM v. Saint Lucia, an ICSID tribunal ordered security for costs. However, the underlying facts in that 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.
>
> Yet, no such exceptional circumstances have been evidenced in the instant case. The Claimants have not defaulted on their payment obligations in the present proceedings or in other arbitration proceedings. The Tribunal is of the view 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 [citations omitted].[49]

In *SAS v. Bolivia*, Bolivia requested the tribunal to order the claimant (allegedly a Bermuda shell company with no assets or economic activity) to provide security for costs in the amount of USD 2.5 million.[50] In its assessment, the tribunal considered four 'basic aspects' *viz.*:

> (i) the Tribunal's powers to order security for costs; (ii) the Tribunal, in deciding a request for security for costs, cannot pre-judge the issues submitted to it for decision; (iii) the standard to grant security for costs; and (iv) whether the mere existence of a third-party funder is sufficient to grant security for costs.[51]

First, the tribunal noted that the authority to order security for costs does not derive explicitly from the UNCITRAL Rules, which were the applicable arbitration rules in the case, nor the *lex arbitri*, which was the Dutch civil procedural law.[52] However, the tribunal stated that 'several decisions of arbitral tribunals in investment arbitrations ... confirm that arbitral tribunals are empowered to order security for costs [citations omitted]'.[53] The tribunal initially concluded that it could not grant security

47. *EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic*, ICSID Case No. ARB/14/14, Respondent's Reply Application for Provisional Measures and Rejoinder Opposition to Claimant's Application for Provisional Measures para. 74 (21 Nov. 2014).
48. *Id.* para. 3.
49. *EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic*, ICSID Case No. ARB/14/14, Procedural Order No. 3 Decision on the Parties' Requests for Provisional Measures, paras 122–123 (23 Jun. 2015).
50. *South American Silver Limited v. Bolivia*, *supra* n. 46, paras 12, 55.
51. *Id.* para. 47.
52. *Id.* para. 51.
53. *Id.* para. 52.

for costs merely on the ground that SAS was used by the 'real investor' to bring a claim.[54] Doing so, the tribunal argued, would constitute a prejudgment on a crucial jurisdictional issue, 'on which Parties' submissions are pending … [which will] enable the Tribunal to analyze the possibilities of success of this defense'.[55] The tribunal continued to address the standards for granting security for costs. It emphasized, *inter alia*, with reference to *RSM v. Saint Lucia*, that:

> In relation to the necessity and the urgency of the measure, investment arbitration tribunals considering requests for security for costs have emphasized that they may only exercise this power where there are *extreme and exceptional circumstances* (emphasis added) that prove a high real economic risk for the respondent and/or that there is bad faith on the part from whom the security for costs is requested. Except for the case of *RSM v. Saint Lucia*, arbitral tribunals in investment cases have refused to order security for costs [citations omitted].[56]

Bolivia based its motion on the allegation that the claimant was in financial distress. However, the tribunal stressed that financial difficulties alone are not sufficient to form the basis for security for costs:

> In sum, the general position of investment tribunals in cases deciding on security for costs is that the lack of assets, the impossibility to show available economic resources, or the existence of economic risk or difficulties that affect the finances of a company are not *per se* reasons or justifications sufficient to warrant security for costs.[57]

The ensuing subject of analysis was whether the existence of TPF was a 'determining factor' in the assessment of security for costs. First, the tribunal established that the existence of TPF per se is a factor that should be considered when deciding security for costs.[58] The tribunal did refer to the above-cited assenting opinion of Gavan Griffith in *RSM v. Saint Lucia*, which indicated that the claimant should carry the burden of proving that the existence of a third-party funder is not an 'exceptional circumstance'. However, it continued stating that '[a]dditionally, in the decision in EuroGas v. Slovak Republic, cited by Bolivia, and which is subsequent to RSM v. Saint Lucia, the tribunal stated that the mere existence of a third-party funder is not an exceptional situation justifying security for costs [citations omitted]'.[59]

Accordingly, the tribunal held that, while TPF is a factor that may be considered in the overall assessment, it is not in and of itself sufficient to base a motion for security for costs.[60] Neither is TPF to be viewed as evidencing the claimant's incapacity to comply with an adverse decision or award, as external funding may be sought for other reasons than purely financial ones.[61] The tribunal denied the motion for security for cost as Bolivia had not proven that:

54. *Id.* para. 55.
55. *Id.*
56. *Id.* para. 59.
57. *Id.* para. 63.
58. *Id.* para. 73.
59. *Id.* para. 74.
60. *Id.* para. 75.
61. *Id.* para. 76.

> SAS is in a situation where it does not want to pay, or that it has breached its obligations, or that it has carried out acts from which the Tribunal may clearly and sufficiently conclude that SAS does not have the means to comply with an eventual award on costs.[62]

In sum, *Eurogas v. Slovak Republic* and *SAS v. Bolivia* support the view that the presence of TPF per se does not constitute an 'exceptional circumstance'. Furthermore, the fact that the funder may not have committed to cover liability for the costs of the adverse party does not automatically lead to the deduction that the claimant is unable to comply with an adverse costs award. Instead, the tribunal must assess the impecuniousness and the details of the funding jointly and cumulatively. This additional layer of analysis leads to the conclusion that impecuniousness in conjunction with the presence of funding may support the assumption that the claimant has limited ability to comply with adverse decisions on costs. Moreover, although impecuniousness and TPF may be important factors, the moving party must prove additional circumstances in order for the tribunal to grant security for costs.

Garcia Armas v. Venezuela (2018)[63]

Garcia Armas v. Venezuela constitutes the second investor-state arbitration case involving TPF where the tribunal granted security for costs. In a procedural order, the tribunal compelled the funded investor to post security for costs amounting to USD 1.5 million. At the outset of its decision, the tribunal assessed the relevance of TPF in relation to the general standards for ordering security for costs. The tribunal held that security for costs should only be ordered in exceptional circumstances and that TPF per se does not constitute proof of insolvency. However, the tribunal also highlighted that the funding agreement (which had been disclosed in full) did not entail any TPF responsibility for adverse costs. Furthermore, the claimants had in general indicated that they possessed a limited ability to cover costs relating to the proceedings (only five out of nine claimants had provided any proof of solvency). As the funder, in addition to this, had not committed to cover any adverse costs, the tribunal deemed it uncertain whether claimant would be able to cover adverse costs awarded to Venezuela.[64] It is interesting to note that – as opposed to the tribunal in *RSM v. Lucia* – the tribunal in this case required actual proof that the funder had not committed to cover adverse costs.

[3] Viewpoints as Expressed in Literature and the Queen Mary Report

The conclusion that TPF per se is not an 'exceptional circumstance' gains support in the literature. The same applies for the tribunal's statement in *SAS v. Bolivia* that resorting

62. *Id.* para. 83.
63. Caso CPA No. 2016-08 *Manuel Garcia Armas v. Venezuela*, Procedural Order No. 9 (Security for Costs) (20 Jun. 2018).
64. The decision is so far only available in Spanish. The facts presented are gathered from a case summary and translation provided in Lisa Bohmer, *Arbitrators Rule that Investors Backed by a Prominent Litigation Funder Must Post USD 1,5 Million Security in Order to Prosecute Investment Treaty Arbitration*, Investment Arbitration Reporter (11 Jul. 2018).

to TPF is not equivalent to being impecunious. For instance, von Goeler has stated that the presence of TPF may enlighten the arbitrators of the financial situation of the claimant in general but he also highlighted that:

> The mere fact that a claimant has entered into a litigation funding agreement should not automatically lead to security payment because this fact is insufficient to deduce that the funded party will not be able to pay an adverse costs award. Neither should the existence of a litigation funding agreement lead to a rebuttable presumption for the claimant's impecuniosity. After all, litigation funding is also used by financially stable parties that simply wish to share risk and maintain liquidity [citations omitted].[65]

He further pointed out that the funding agreement may provide that the third-party funder will cover a possible adverse costs award. In those cases, the presence of TPF would, in fact, constitute a compelling argument against granting security for costs.[66] This view gains additional support from Laurent Lévy and Regis Bonnan who have written that '[t]he funded party's insolvency may not suffice to warrant an order for security for costs, and the possibility or fact that the concerned party is "funded" should thus in principle not be decisive either'.[67]

The Report of the International Council for Commercial Arbitration (ICCA)-Queen Mary Task Force on Third-party Funding in International Arbitration thoroughly discusses the connection between TPF and the standards for security for costs.[68] The report constitutes a detailed and well-founded analysis by a reputed task force composed by the leading experts from various professional backgrounds of TPF-related issues and the report should – and likely will – carry significant weight as 'soft law' going forward. The report addresses provisions on security for costs of prominent arbitration laws and arbitration rules, as well as relevant arbitration practice and doctrinal developments. In the concluding recommendations of the report, it is stated that an 'application for security for costs should, in the first instance, be determined on the basis of the applicable test, without regard to the existence of any funding arrangement'.[69] The reason behind this approach is in part that the Task Force acknowledges that the fact that a party is using TPF is not itself evidence that the party is impecunious.[70] The views expressed by von Goeler (member of the Task Force), in this regard, are supported by the report's conclusions which emphasize that:

> [T]he 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.[71]

65. Jonas von Goeler, *supra* n. 1 at 341.
66. *Id.* at 342.
67. Laurent Lévy and Regis Bonnan, *supra* n. 27 at 80.
68. *See* Report for public discussion of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration, Apr. 2018. The ICCA Reports No. 4.
69. *Id.* at 16.
70. *Id.* at 171.
71. *Id.* at 180.

This, in turn, constitutes a compelling argument against the view (advocated, e.g., by Gavan Griffith in *RSM v. Saint Lucia* as discussed above) that the mere existence of funding triggers a presumption of impecuniosity.[72] Moreover, the assessment of the Task Force supports the view articulated in arbitration practice, i.e., that funding and impecuniousness per se may not form the basis for an application for security for costs.

The report further underlines the significance of the terms of the funding agreement for the assessment of the claimant's ability to comply with an adverse costs award. It states that '[t]he terms of any funding agreement … may be relevant if relied upon to establish that the claimant (or counterclaimant) can meet any adverse cost award (including, in particular, the funder's termination rights)'.[73] According to the Task Force, there are two elements of the funding agreement that are relevant for the funded party's ability to comply with an adverse costs award. The first is whether the funding agreement includes an obligation for the funder to cover adverse costs. If such an obligation is in place, there is arguably no need for the claimant to post security for costs.[74] The second factor relates to the funder's termination rights. The funder's commitment to cover adverse costs is redundant if the funder may terminate the funding agreement at any time and, by doing so, is relieved of its obligations.[75]

[4] Summarizing Notes on Security for Costs

In conclusion, when applying for security for costs under the SCC Rules, it is clear that the essential criterion is for the moving party to prima facie prove inability to comply with an adverse costs award. Due to the limited application of Article 38 of the SCC Rules on security for costs in practice, it is uncertain how to interpret the article in relation to cases involving TPF. However, the prevalent view derived from international practice and other sources of soft law nature appears to be that the respondent must present evidence as to why the claimant – based on an overarching assessment – is unable to cover costs awards in order for security for costs to be granted. Impecuniousness, naturally, may affect a party's capacity in this respect. Still, the fact that a party is funded does not necessarily entail that the party is impecunious, as far from all funded parties are impecunious. Neither does it automatically mean that the party is unable to comply with a costs award, as the funder may have committed to provide such coverage in case the funded party proves unable to do so. Thus, proving the existence of TPF per se, should in most cases not suffice for acquiring security for costs. Instead, evidence supporting the claimant's incapacity may be constituted by records showing that the party has a history of failing to comply with costs orders. Furthermore, remarks by scholars and practitioners, as well as international case law, suggest that the specific terms of the funding agreement may have a significant impact on the tribunal's assessment. Most importantly, whether the funding agreement entails that

72. *Id.*
73. *Id.* at 16.
74. *Id.* at 181.
75. *Id.*

the funder will cover adverse costs is of significant importance when assessing the funded party's overall capacity to cover an adverse costs award. The same is true as regards the conditions in the funding agreement regarding termination. If the funding agreement provides a unilateral opportunity for the funder to terminate the agreement and evade its obligation to cover adverse costs, the funded party's capacity to cover adverse costs diminishes significantly.

[B] Disclosure in Relation to Security for Costs

With respect to the relation between disclosure orders and security for costs, the SCC Rules and practice provide little guidance. Also from a global viewpoint, there is relatively little case law and scholarly commentary on the issue of to what extent tribunals may order disclosure for the purpose of properly assessing the standards for granting security for costs in cases involving TPF. One occurring argument in support of ordering disclosure of the funding agreement is that the tribunal must be enlightened about the details behind the funding in order to properly assess the need of such measures.[76] In other words, the tribunal may need details about specific funding terms to assess the claimant's ability to comply with an adverse costs award. Those were in part the reasons applied by the tribunal in *Muhammet Cap v. Turkmenistan* which constitutes the first case where a tribunal ordered disclosure to assess the need for security for costs.[77] The tribunal imposed a quite extensive disclosure requirement vis-à-vis the funded claimant. In its assessment, the tribunal put emphasis on the respondent's suspicion or 'concern', as well as the fact that the claimant had refrained from repudiating the respondent's allegation that the claimant had previously been unable to comply with costs orders. In the view of the tribunal, these circumstances were sufficient to merit disclosure of the funder's identity, as well as the 'nature' of the funding relationship.[78]

The tribunal in *Guarachi v. Bolivia*, however, rejected the same line of argument. There, the tribunal found the information of the funder's identity as sufficient for the purpose of declaring the absence of any relations between the funder and the members of the panel. Thus, the motivation for ordering disclosure was not the request for security for costs, but instead related to conflicts of interest.[79] A similar line of reasoning was applied in *SAS v. Bolivia* (discussed above) where the tribunal ordered disclosure in order to enhance transparency while refusing to accept the motion for security for costs as constituting the basis for disclosure.[80] The tribunal in *Garcia Armas v. Venezuela* on the other hand, recognized the terms behind the funding as of

76. Maxi Scherer, *Third-Party Funding in International Arbitration Towards Mandatory Disclosure of Funding Agreements?,* Ch. 8 in *10 Third-Party Funding in International Arbitration (ICC Dossier)* 96 (Bernardo M. Cremades Sanz-Pastor & Antonias Dimolitsa eds, 2013).
77. *See Muhammet Cap & Sehil In_aat Endustri ve Ticaret Ltd. Sti. v. Turkmenistan*, ICSID Case No. ARB/12/6, Procedural Order No. 3 (15 Feb. 2013).
78. *Id.* para. 13.
79. *See Guaracachi America Inc. and Rurelec PLC v. The Plurinational State of Bolivia*, UNCITRAL, PCA Case No. 2011-17, Procedural Order No. 13 para. 9 (21 Feb. 2013).
80. *SAS v. Bolivia*, *supra* n. 46, para. 79.

high importance in relation to security for costs. It went further than the tribunal in *Muhammet Cap v. Turkmenistan* and ordered disclosure of the funding agreement in full. The order relied on the alleged necessity of determining whether the funder had committed to cover adverse costs. As noted above, what became subject to disclosure also laid the basis for the tribunal's final decision on security for costs.[81]

The relation between disclosure orders and security for costs is commented in literature to some extent. von Goeler has stated that:

> [D]isclosure of funding-related facts to the tribunal and the opponent may be required to assess a security for costs request. In this regard, the funding agreement should be treated like any other piece of documentary evidence not in possession of the requesting party but which may be needed to assess the security request, such as annual accounts, statutory returns, or other unpublished past and present financial records of the claimant. This means that a funded party should not be obliged to disclose facts related to the funding agreement *sua sponte* when it comes to security for costs. The requesting party must show a reasonable belief of a third-party funding agreement's existence, reasonably specify that agreement, substantiate which terms of the agreement may be relevant and material to its submission, and overcome potential privilege defences raised in the particular case.[82]

As demonstrated in the decision in *Garcia Armas v. Venezuela*, a tribunal may find it appropriate to order disclosure of the funding agreement for the purpose of assessing the need for posting security for costs. However, similar to when deciding whether or not to grant security for costs, the existence of TPF per se likely should not suffice to warrant disclosure of the terms of the agreement. As argued by von Goeler, it appears more sensible to demand the respondent to specifically account for the relation between the requested information and the applicable standards for granting security for costs. Arguably, information regarding whether the funding agreement provides that the funder has committed to cover adverse costs is information that typically influences the claimant's ability to cover an adverse costs award. This in turn, directly influences the assessment of security for costs which may merit disclosure of such information.

As discussed above, the view that the terms of the funding agreement may be relevant for security for costs applications gains additional support from statements of the Queen Mary Task Force. Moreover, in cases where the funded party is impecunious, the report states that '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'.[83] In the view of the Task Force, such an obligation of the funded party, however, appears overly burdensome if the disclosure obligation refers to the entirety of the funding agreement. In light of that, it is suggested that the scope of the obligation ought to be limited to the funded party testifying to whether the funder

81. Lisa Bohmer, *supra* n. 64.
82. Jonas von Goeler, *supra* n. 1 at 339–340.
83. *See* Report for public discussion of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration, Apr. 2018. The ICCA Reports No. 4, at 181.

is obligated to cover an adverse costs award. To promote efficiency, this could be accomplished through, e.g., an affidavit or witness statement.[84]

Summarizing the prevalent views on this issue, it seems clear that the relevance of the terms of the funding agreement as to the claimant's capacity to comply with an adverse costs award also impacts the scope of disclosure orders. A party moving for security for costs may need assurances as to whether – and to what extent – the third-party funder covers adverse costs. In such a situation, it is arguably within the tribunal's discretion to order the claimant to disclose that information. However, contrary to what the tribunal held in *Garcia v. Venezuela*, such a disclosure order should refer only to terms relevant for assessing the funded party's ability to cover adverse costs and not the funding agreement in its entirety.

§10.04 CONCLUDING REMARKS

The utilization of security for costs may serve the purpose of mitigating the negative aspects related to a non-funded party's ability to obtain costs reimbursement when faced with TPF-backed arbitration claims brought by an impecunious adversary. However, based on arbitration practice, theory and doctrinal developments, the mere presence of TPF and impecuniousness should not suffice as basis for an order for security for costs. Nonetheless, the contents of the funding agreement may serve as an important factor in the tribunal's overall assessment.

In order for a tribunal to properly assess the need for issuing a security for costs order, it may need to be informed of circumstances that bear relevance to the funded party's ability to cover an adverse costs award. For this purpose, a tribunal may be justified in ordering an impecunious party to disclose the existence of funding and even terms of the funding agreement. However, the scope of a disclosure order of this kind should never extend beyond terms that are relevant for evaluating the party's capacity to comply with an adverse costs award. Furthermore, as suggested by the Queen Mary Task Force, a viable alternative to full disclosure would be that the funded party, preferably in a witness statement or affidavit, answers questions posed by the tribunal regarding the funder's responsibility to cover adverse costs.

Finally, as demonstrated particularly by the debate ensuing *RSM v. Saint Lucia*, the queries surrounding disclosure and security for costs in TPF arbitration have given rise to controversy. Statements of the kind of Gavan Griffith in *RSM v. Saint Lucia* expressing general scepticism towards the use of TPF are not uncommon. Yet, sometimes they appear to rely solely on the false premise that TPF per se is an unethical and opportunistic practice. Concurrently, on the other side of the view spectrum, arbitrators engaging in a more business-oriented approach may excessively promote a *laisses-faire* attitude that carries the risk of overlooking any potentially negative procedural inferences of TPF. The apparent 'clash' raises concerns vis-à-vis the absence of guiding general legal principles or rules. In light of this rule absence and notable lack of consensus, relying entirely on arbitrators to make decisions relating to

84. *Id.*

security for costs carries the risk of impeding foreseeability while simultaneously vitalizing arbitrariness. This has already been clearly demonstrated in the tangible inconsistency shown in international practice. Perhaps, reconciling the view of the sceptics with the advocates for business efficiency requires more guiding standards. In light of this, the Queen Mary Task Force's endeavour is a welcomed one, which may constitute a step towards a clearer and universal approach.