Third-Party Funding in International Arbitration: Useful Experience from Australia

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ABSTRACT

Australia is renowned as a leading jurisdiction for litigation funding, underpinned by an expanding market and generally supportive legislature and judiciary. Less clear is the Australian approach to third-party funding in international arbitration. In an exploration of the Australian litigation funding landscape, this article seeks to understand whether any lessons can be gleaned in addressing the growing role of third-party funding in international arbitration. Through a consideration of the discrete issues of disclosure, confidentiality, costs orders, and security for costs, it is clear that both the Australian and international responses to litigation funding offer valuable guidance on issues surrounding third-party funding in international dispute resolution.

1 INTRODUCTION AND BACKGROUND

Consider the situation where a dispute over claims for delay between two construction companies is to be referred to international arbitration. In this case the claimant has a meritorious claim against the respondent, but either the claimant's financial capacity is significantly more limited than the respondent's or the claimant needs to commit its cash flow to alternative business critical projects. Given the potential for large-scale international arbitration proceedings to be a costly and protracted affair (which, regrettably, is sometimes the case), it has become a reality that in these circumstances claimants are left with little choice but to forego enforcement of their legitimate rights. This is clearly an unsatisfactory situation. It is this problem that is driving the growth in markets for litigation financiers who offer the financial resources needed to enforce these rights.

Third-party funding therefore refers to the scenario whereby a party with no prior interest in a dispute provides a financial contribution to a party (usually the claimant) to support their claim. This funding is provided on the proviso that, if the party is successful in its claim, the funder will receive a proportion of the claimed sums. In the event that the claiming party is unsuccessful in its claim, the

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existence of ATE insurance, as well as contractual indemnity clauses, will typically protect the claimant from the effects of an adverse costs order. Thus, third-party funding is considered to be a valuable service for disputing parties as it allows them to minimize the risk associated with instigating proceedings, preserve cash flow for other endeavors, and ensures that counsel remain remunerated.[1] Nevertheless, while following this basic structure, the nature of third-party funding agreements can vary significantly, with third-party funders having varying degrees of control and involvement in the proceedings.

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Last year, the intrigue surrounding third-party funding in international arbitration swelled with the release of the ICCA-Queen Mary Task Force Report on Third-Party Funding in International Arbitration (the "ICCA-Queen Mary Report").[2] The publication provides a response to the growing significance of the third-party-funding industry in international arbitration and the complex challenges that have developed alongside this growth. There has been much speculation as to the source of this rapid growth, with suggestions including that it has been powered by a global deregulation of the legal profession,[3] a response to the global financial crisis,[4] or the reputation of arbitration as a costly exercise.[5] Regardless, third-party funding now requires the attention of the international arbitration community. However, this is not entirely uncharted territory. For instance, these challenges are not unknown to Australia, a jurisdiction where litigation funding has overcome many teething issues and seen considerable growth in the twenty-first century.

Thus, this article considers the current development of the Australian litigation funding market – renowned as one of the most progressed in the world – particularly focusing on advances in the regulation of litigation funding and the approach of the Australian judiciary to funding arrangements. With this understanding, the paper then turns to consider the Australian approach to salient issues in litigation funding, contrasting these with international responses and considering whether they offer any guidance for international arbitration. In this regard, the article considers the Australian approach to the following issues:

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1 *ICCA-Queen Mary Task Force Report on Third-Party Funding in International Arbitration* (International Council for Commercial Arbitration, 2018) (hereinafter "ICCA-Queen Mary Report"); Nicholas Rowles-Davies and Jeremy Cousins, *Third Party Litigation Funding* 62 (Oxford University Press, 2014).

2 ICCA-Queen Mary Report at 18.

3 *See* Catherine Rogers, *Gamblers, Loan Sharks & Third-Party Funders* 3 (Pennsylvania State University and Dickenson School of Law Legal Studies Research Paper No. 51, 2013).

4 ICCA-Queen Mary Report at 18.

5 *See e.g.* Queen Mary University of London and White & Case, *2018 International Arbitration Survey: The Evolution of International Arbitration* 8 (2018); 67 percent of respondents indicated that cost was one of the three worst characteristics of international arbitration.

– first, obligations of disclosure of third-party funding and the balancing of party confidentiality against the need to maintain the legitimacy of the international arbitral process; and
– second, issues of costs and security, including the viability of costs orders against non-parties to the dispute, and the role of security for costs where a third-party funder is involved.

A normative discussion of the particular features of third-party funding and its role in international arbitration is largely beyond the scope of this article. Rather, the article adopts a more practical focus, exploring the development of the Australian approach to third-party funding in an attempt to understand whether the Australian domestic approach has any relevance to international arbitration. The author believes that this is of value as such practical considerations can often be overlooked in the larger normative debate.

2 THIRD-PARTY FUNDING IN AUSTRALIA

The Australian attitude to third-party funding tends towards what has been called the "market-oriented approach,"[6] which accepts that potential claimants may explore the wider market to support their claims and emphasizes the merits of third-party funding as a means of access to justice. This stands in stark opposition to countries like Brazil, Ireland, and Sweden, which have historically leaned towards a "true claimant" approach, disfavoring third-party funding and preferring that claims be supported only by the "actual" claimant to the proceedings.[7]

A consequence of this is that Australia is renowned for possessing one of the most developed litigation funding markets in the world, spanning a twenty-year history.[8] In 2015, IMF Bentham estimated the Australian litigation funding market to be worth AUD 3 billion, representing, by their estimations, approximately 14 percent of the Australian litigation market.[9] Much of this growth can be seen in the class action sphere, with the Victorian Law Reform Commission ("VLRC") finding last year that almost half of class actions filed in the Federal Court of

[6] Daniel Kaldermis and Paula Gibbs, *Third-party funding in international arbitration – lessons from litigation?*, Kluwer Arbitration Blog (December 15, 2014), http://arbitrationblog.kluwerarbitration.com/2014/12/15/third-party-funding-in-international-arbitration-lessons-from-litigation/.

[7] *Ibid.*

[8] *See* George R. Baker, *Third-Party Litigation Funding in Australia and Europe* (2012) 8(3) *Journal of Law, Economics and Policy* 451, 452; Valentina Frignati, *Ethical Implications of Third-Party Funding in International Arbitration,* (2016) 32(1) *Arbitration International* 506; ICCA-Queen Mary Report at 18.

[9] *See* Jason Geisker and Jenny Tallis, *Australia*, in *The Third Party Litigation Funding Review* 11, 11 (Leslie Perrin ed., 2d ed., Law Business Research, 2017), citing IMF Bentham, *Litigation Funding Masterclass* 8 (October 2015), https://www.imf.com.au/docs/default-source/site-documents/investor-presentation---litigation-funding-masterclass360804010281659d9b61ff00006a85af.pdf.

Australia were supported by a third-party funder.[10] The VLRC found that this significant growth has not been universal, however, and that uptake had been slower in other courts, including the Victorian Supreme Court, where only ten out of eighty class actions brought involved a third-party funder.[11]

In common law jurisdictions, the doctrines of maintenance and champerty have historically operated to prevent third-party funding of litigation. Established in medieval England, the doctrine of maintenance makes it a criminal offense for an uninterested third party to maintain or encourage a lawsuit. Champerty, a form of maintenance, further prohibits uninterested third parties from paying legal costs in return for proceeds from the dispute. In Australia, the doctrines of maintenance and champerty have been abolished as crimes and torts in New South Wales,[12] Victoria,[13] South Australia,[14] and the Australian Capital Territory.[15] However, this did not mean that litigation funding agreements were impervious to challenge, as, despite the abolition of these doctrines, challenges could still be made against litigation funding agreements based on arguments that they were contrary to public policy.[16] This meant that it was not until 2006, when the High Court of Australia affirmed the legitimacy of third-party funding in *Campbells Cash & Carry Pty Ltd v. Fostif Pty Ltd* ("*Fostif*"), that the development of the industry was assured.[17] *Fostif* considered a representative proceeding claiming recovery of amounts paid by tobacco retailers to tobacco wholesalers. The tobacco retailers had made these payments for the purposes of allowing the wholesalers to pay a licensing fee, which was later found to be unconstitutional. A litigation funder commenced these proceedings, seeking a third of any sums recovered. In that case, the court held that litigation funding did not give rise to a permanent stay of proceedings on the grounds of an abuse of process, nor for reasons of public policy. The case is therefore recognized as affirming that in those jurisdictions where maintenance and champerty had been abolished proceedings could not be successfully challenged merely due to the existence of a litigation funding arrangement. Thus, commentators herald *Fostif* as responsible for "entrenching" third-party funding in Australia.[18] It follows from *Fostif* that litigation funding has become accepted in the Australian legal system, prompting its move from the periphery to a tool readily deployed in the Australian legal market.

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10 Victorian Law Reform Commission, *Access to Justice – Litigation Funding and Group Proceedings: Consultation Paper* 8 (2017).
11 *Ibid*.
12 *Maintenance, Champerty and Barratry Abolition Act 1993* (NSW).
13 *Abolition of Obsolete Offences Act 1969* (Vic).
14 *Criminal Law Consolidation Act 1935* (SA) sch. 11; this schedule was inserted in 1992.
15 *Statute Law Amendment Act 2002* (ACT).
16 *Anstella Nominees Pty Ltd v. St George Motor Finance Ltd* [2003] FCA 466.
17 (2006) 229 CLR 386.
18 See Geisker and Tallis, *supra* note 9 at 12.

With this understanding, it must be considered whether any guidance can be garnered from the Australian experience of salient issues in domestic litigation funding.

3 SALIENT ISSUES

3.1 Disclosure of Third-Party Funders and Third-Party Funding Agreements

The first pertinent area of regulation in third-party funding arrangements is the question of disclosure of the existence, identity, and details of a third-party funder when they are providing financial assistance to a party. These issues of disclosure present challenges in balancing transparency against the need to protect the party's commercially sensitive information. In this section, this article looks to the Australian legislative and judicial approach to disclosure of litigation funding arrangements to ascertain whether such approaches are transplantable to similar disclosure issues in international arbitration.

At the outset, it is useful to explore the contents of a third-party funding arrangement, the centerpiece of which is the agreement that the funder will pay the funded party's costs in exchange for a share of any sums recovered.[19] The ICCA-Queen Mary Report elaborates that a third-party funding agreement usually contains "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."[20] The agreement therefore contains several elements of essential information and conditions concerning the amount of the investment, the return, and the prescribed conduct of the third-party funder and the funded party. Often of particular recognition are clauses pertaining to the grounds for termination of funding by the funder, which have frequently attracted the courts' attention as being commercially sensitive.

It is beyond the scope of this paper to enter into a normative discussion of the merits of disclosure of details of third-party funding, aside from remarking that it is becoming generally accepted that disclosure of the identity of the third-party funder is a necessity to ensure the legitimacy and efficiency of international arbitration;[21] only through disclosure are arbitrators able to fulfill their own

[19] *See* Jonas von Goeler, *Third-Party Funding in International Arbitration and its Impact on Procedure* 1–19 (Kluwer Law International, 2016).

[20] *See* ICCA-Queen Mary Report at 32.

[21] *See* Goeler, *supra* note 19 at 135; Catherine Rogers, *Ethics in International Arbitration* 201 (Oxford University Press 2014); Catherine Rogers, *A Trend Towards Mandatory Disclosure of Third Party Funding?*

disclosure and impartiality obligations.[22] In response to these calls, domestic legislation,[23] institutional rules,[24] free-trade agreements,[25] and soft law instruments[26] have all been deployed, with varying success, as mechanisms to compel disclosure where a third-party funding agreement exists.

3.1[a] Disclosure of Litigation Funding Agreements in Australian Case Law

Given the supportive environment for third-party funders that exists in Australia, it comes as little surprise that Australian courts have generally been opposed to revealing the details of a litigation funding agreement – an opposition that appears to be rooted in a concern that divulging such details may provide defendants with a strategic or tactical advantage.[27] Indeed, as was noted by Goldberg J in *Re Kingshealth Club of Clubs Ltd* (2003), "a litigant is not normally privy to the 'war chest' that the opposing party has available to fund the litigation,"[28] and so for the Australian courts it is logical that the defendant should also not be given access to the "war chest" of the plaintiff merely because it is in another's possession.[29] In that case Goldberg J was concerned that upon discovering the gold, or lack thereof, at the plaintiff's disposal, the defendants would be able to assess and implement strategies to "eat up" the litigant's funding prior to the conclusion of the trial.[30] Australian courts therefore possess a penchant for privacy, but to understand the nature and extent of the Australian courts' commitment to this protection it is necessary to look towards two pertinent Australian cases.

First, the decision of the New South Wales Supreme Court in *Weston v. Publishing and Broadcasting Ltd* (2010) demonstrates an occasion where an Australian court has taken extensive steps to preserve the confidentiality of a litigation funding agreement. In that case the defendants sought the removal of confidentiality orders that had been placed over material produced in connection with an *ex parte* application. Amidst this material was a litigation funding

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Recent Developments and Positive Impact, Kluwer Arbitration Blog (May 2, 2016), http://arbitrationblog.kluwerarbitration.com/2016/05/02/a-trend-towards-mandatory-disclosure-of-third-party-funding-recent-developments-and-positive-impact/.

22 *See* ICCA-Queen Mary Report at 85, 98.

23 e.g., *Arbitration and Mediation Legislation (Third Party Funding)(Amendment) Ordinance 2017*, s. 98U (Hong Kong); *Legal Profession (Professional Conduct) Rules 2015*, r. 49A (Singapore).

24 e.g., *SIAC Investment Arbitration Rules 2016*, r. 24(1).

25 e.g., *EU-Vietnam Free Trade Agreement*; *Comprehensive Economic and Trade Agreement* (CETA), http://ec.europa.eu/trade/policy/in-focus/ceta/ceta-chapter-by-chapter/.

26 e.g., *IBA Guidelines on Conflicts of Interest in International Arbitration*, General Standard 6(b), 14 (International Bar Association 2014).

27 *See Re Addstone Pty Ltd (In Liq)* (1998) 83 FCR 583.

28 [2003] FCA 1034, [33] (Goldberg J).

29 *Ibid*.

30 *Ibid*.

agreement made between the plaintiffs and their funder, and so the defendants sought to review these documents to support their own independent motion. Barrett J found that, while the confidentiality orders should be suspended, the defendants should not be given access to the litigation funding agreement, on the grounds that it was necessary that the funding agreement be withheld to secure the proper administration of justice.[31] In Barrett J's mind, the threat to justice came in the form of releasing information that would provide the defendant with a tactical advantage in forthcoming litigation. Thus, the material withheld pertaining to the litigation funding agreement was significant, including the agreement, negotiations, and discussions pertaining to the agreement, and even the identity of the funder.[32]

More recently, a similar dispute was raised in the Federal Court of Australia in *Coffs Harbour City Council v. Australian and New Zealand Banking Group Ltd*, albeit with a somewhat more nuanced approach to balancing issues of confidentiality and transparency.[33] In this case the plaintiffs had previously been ordered to disclose their litigation funding agreement. This order had been made by Wigney J in accordance with the now revoked Federal Court Practice Note CM-17, which provided:[34]

> At or prior to the initial case management conference each party will be expected to disclose any agreement by which a litigation funder is to pay or contribute to the costs of the proceeding, any security for costs or any adverse costs order. Any funding agreement disclosed *may be redacted to conceal information which might reasonably be expected to confer a tactical advantage on the other party*. [Court's emphasis]

The plaintiffs asserted that, consistent with CM-17, they were entitled to redact the litigation funding agreement. This was said to be for two reasons: legal professional privilege and/or a right to confidentiality. Rares J found that, consistent with earlier authority,[35] the litigation funding agreement would not be protected by professional privilege as its contents were not created primarily for the purpose of use in proceedings or for legal advice. With regards to the confidentiality argument, it was noted that the purpose of CM-17 was to ensure a balance between an "expectation of some transparency" and the need to protect commercially sensitive information. Accordingly, Rares J allowed redaction of some content but in a much more limited form than in *Weston*, instead allowing

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31 [2010] NSWSC 1288, [38] (Barrett J).

32 *Ibid.*

33 [2016] FCA 306 (hereinafter "*Coffs Harbour*").

34 Federal Court of Australia *Practice Note CM 17: Representative proceedings commenced under Part IVA of the Federal Court of Australia Act 1976* (Cth), October 9, 2013, s. 3.6.

35 *See Marshall v. Prescott* [2013] NSWCA 152, [85]–[88] (Barrett JA, McColl and Ward JJA agreeing); *CSR Ltd v. Eddy* (2008) 70 NSWLR 725, 740, [66] (Basten JA, Hodgson and McColl JJA agreeing); *Cook v. Pasminco Pty Ltd (No. 2)* (2000) 107 FCR 44, [47] (Lindgren J).

disclosure of the identity of the funder and several standard form clauses, including those pertaining to financial matters, which he deemed could not be exploited by the defendants.[36]

Therefore, at the very least, the position under Australian case law is that elements of the litigation funding agreement will be considered confidential where their disclosure would present the defendant with the opportunity to use that information for the purposes of a tactical advantage. At its broadest, the confidentiality of the entire litigation funding agreement and the identity of the funder will be considered confidential to protect the interests of the parties.

3.1[b] Other Australian Developments Pertaining to an Obligation of Disclosure

Nevertheless, recent developments in soft law material in Australia have illustrated a trend toward favoring disclosure of the identity and at least parts of litigation funding agreements where a funder is involved. Such a position has been particularly embraced in the sphere of litigation funding of class actions.

The Federal Court of Australia has led the way in this area. For instance, Practice Note CM-17,[37] referred to in *Coffs Harbour*, was revoked in 2013 and replaced with the Class Action Practice Note ("GPN-CA"),[38] Part 6 of which prescribes clearer disclosure obligations and categories of exceptions for solicitors engaged in class action matters in the Federal Court. Pursuant to Part 6, solicitors are obliged to provide any litigation funding agreement to the court prior to the first case management hearing in a confidential setting.[39] Crucially, solicitors also have an obligation of disclosure to the other parties involved in the dispute and must provide a "Notice of Disclosure - Litigation Funding Agreements." This may be limited to an example of the standard form agreement or be redacted to conceal information which might be "reasonably expected to confer a tactical advantage on another party."[40] What confers such a tactical advantage will be informed by the further development of Australian case law.

This movement has also begun to spread into other areas of the Australian judicial system. For instance, in a March 2018 report into litigation funding, the VLRC recommended that the Victorian Supreme Court should amend its practice

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36 *Coffs Harbour*, [25]–[30] (Rares J).

37 See *supra* note 34.

38 Federal Court of Australia, *Class Actions Practice Note (GPN-CA): General Practice Note,* October 25, 2016 (hereinafter "GPN-CA").

39 *Ibid*. s. 6.1; the notice of disclosure form is available at http://www.fedcourt.gov.au/forms-and-fees/forms/ncf#ncf3.

40 GPN-CA s. 6.4.

note on class actions to mirror Part 6 of its Federal Court equivalent.[41] In that report, the VLRC also advocated a similar disclosure regime for litigation funding agreements in all proceedings before the Victorian Supreme Court where third-party funders are involved.[42] Thus, the VLRC has signaled a movement in Australia towards greater disclosure obligations. Yet the extent to which this will manifest remains largely unclear.

3.1[c] International Approaches and Applying the Australian Position to International Arbitration

These developments raise the relevant question of whether the obligations of disclosure pertaining to litigation in Australia should be extended to international arbitration. This position received some support from a discussion paper released by the Australian Law Reform Commission ("ALRC") in May 2018, wherein it was recommended that obligations of disclosure akin to those contained in the GPN-CA should be extended to other forms of dispute resolution, including arbitration.[43] The ALRC stated that it was "preferable that the obligations on solicitors in relation to the disclosure of third-party funding in all forms of dispute resolution should be aligned" and that it was nonsensical for these obligations to be confined to litigation.[44] The paper noted that, while the ACICA Rules (2016) do not impose any obligation of disclosure in relation to third-party funding arrangements, "the international trend is to require such disclosure."[45]

This is no doubt a reference to recent developments in Singapore, France, and Hong Kong, which have each recently taken steps to liberalize third-party funding in the arbitration sphere[46] and concurrently moved to impose obligations of systematic disclosure. In Hong Kong, an amendment to the Arbitration Ordinance will oblige parties, at the commencement of the arbitration, to give notice to the other party and the arbitral institution of both the existence of an arbitration agreement and the identity of the third-party funder.[47] In the event that a third-party funding agreement is entered into after the commencement of the arbitration, the parties must produce these details within fifteen days of the

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41 Victoria Law Reform Commission, *Access to Justice – Litigation Funding and Group Proceedings: Report* xix (March 2018).

42 *Ibid*.

43 Australian Law Reform Commission, *Inquiry into Class Action Proceedings and Third-Party Litigation Funders*, Discussion Paper No. 85 (2018) (hereinafter "ALRC DP 85").

44 *Ibid*. at 78.

45 *Ibid*. at 79.

46 Christine Sim, *Third Party Funding in Asia: Whose Duty to Disclose?*, Kluwer Arbitration Blog (May 22, 2018), http://arbitrationblog.kluwerarbitration.com/2018/05/22/third-party-funding-asia-whose-duty-disclose/.

47 *Arbitration and Mediation Legislation (Third Party Funding)(Amendment) Ordinance 2017*, s. 98U.

agreement being made.[48] Meanwhile, Singapore has also developed these obligations, albeit in a different fashion, imposing obligations of disclosure upon counsel rather than the parties. Under the Legal Profession (Professional Conduct) Rules, practitioners are obliged to reveal the existence of any third-party funding agreement and the identity and address of the third-party funder "as soon as practicable" after entry into the agreement.[49] On a strict reading, this obligation will likely not apply to foreign counsel. Therefore, despite their different focuses, the Hong Kong and Singapore regimes are largely similar, compelling disclosure from the outset of the arbitration. Finally, in March 2017, the Paris Bar Council also endorsed third-party funding.[50] As part of this endorsement, the resolution made by the Paris Bar Council suggests that, where a third-party funder is involved, lawyers should encourage their clients to disclose this fact to the tribunal and other party to avoid any future enforcement issues. Thus, across all three jurisdictions, there has been a movement towards disclosure but it remains questionable whether parties will ever be required to disclose the contents of their third-party funding agreements and, if so, what factors will pertain to any further disclosure. Nevertheless, these recent changes are largely in line with the results of the ICCA-Queen Mary Report which posited two pertinent principles of disclosure: first, that parties should disclose, at the first opportunity, the existence of a third-party funding agreement (termed "systematic disclosure"); and second, that the tribunal has powers to order disclosure of a third-party funding agreement.[51]

The Australian and international experience with third-party funding therefore presents multiple pathways upon which Australia could embark to regulate disclosure of third-party funding in international arbitration. The first is to follow the lead of Singapore and Hong Kong and oblige systematic disclosure of the existence of a third-party funding agreement. Australia could look to enshrine a provision similar to that contained in other jurisdictions or in Part 6 of the GPN-CA into its International Arbitration Act 1974 (Cth). This would mimic the approach of Hong Kong and ensure that the obligation applies to all arbitrations concluded under Australian law. Alternatively, following the advice of the ALRC,[52] the Australian Solicitors' Conduct Rules could be amended to oblige disclosure in all forms of dispute resolution, including arbitration. This would place the obligation of disclosure on counsel rather than the parties and may have a more limited reach than the first pathway. Alternatively, rather than mandating systematic

48 *Ibid*.
49 *Legal Profession (Professional Conduct) Rules 2015*, r. 49A.
50 Sabina Adascalitei, *Paris Bar Council Welcomes Third Party Funding*, CIArb News (June 1, 2017), http://www.ciarb.org/news/ciarb-news/news-detail/features/2017/06/01/paris-bar-council-welcomes-third-party-funding.
51 ICCA-Queen Mary Report at 81.
52 ALRC DP 85 at 78–79.

disclosure, Australia could instead amend its International Arbitration Act 1974 to simply empower tribunals to order disclosure where they deem it appropriate. Thus, it appears that a close study of the Singaporean and Hong Kong regimes will be crucial before Australia moves to consider the merits of any regulation of disclosure of third-party funding in international arbitration.

3.2 Costs Orders against Third-Party Funders and Security for Costs

A second pertinent area of consideration arising in the sphere of third-party funding is the tribunal's ability to award costs. Much of this difficulty stems from the fact that arbitral tribunals are typically limited in their ability to order third parties to bear the costs of an arbitration due to the consensual nature of their jurisdiction.[53] Domestic courts avoid this constraint by virtue of their procedural rules, which may allow them to produce costs orders requiring that non-parties meet procedural costs. For arbitral tribunals, where a third-party funder is involved, questions are therefore raised as to the recoverability of third-party funder costs, the awarding of security for costs, and the ability of the tribunal to order costs awards against third-party funders.

3.2[a] Costs Orders against Third Parties and Security for Costs in Australian Case Law

3.2[a][i] Costs Orders against Non-Parties

The Australian courts have displayed a mixed and even unwilling approach to making costs orders against third-party funders. In New South Wales, the Civil Procedure Act 2005 (NSW) prevents the rendering of a costs order against non-parties, unless their conduct amounts to an abuse of process.[54] In *Jeffrey & Katauskas Pty Ltd v. SST Consulting Pty Ltd*,[55] the High Court of Australia found that the mere fact that a third-party funder did not agree to meet the costs of an adverse costs order did not render their funding of a claimant an abuse of process.[56] Thus, the decision embodies the difficult threshold that parties will have to traverse to gain a costs order against non-parties in New South Wales proceedings. A different result was reached by the High Court in *Knight v. FP Special Assets Ltd*,[57] where the court found that, pursuant to Queensland legislation, it could make a costs order against non-parties where the present party

[53] ICCA-Queen Mary Report at 161.
[54] *Civil Procedure Act 2005* (NSW) s. 42.3(1)–(2), s. 98(1)(a).
[55] [2009] HCA 43.
[56] *Ibid.*
[57] (1992) 174 CLR 178.

to the dispute was plainly unable to meet the costs order. The court posited that this could be due to situations of insolvency or plain incapability of fulfilling the costs order, for instance where the party was nothing more than a straw figure.[58] More recently, it was confirmed in the Western Australian Supreme Court that a costs order can be rendered against a third-party funder as an "interested non-party." This spread of cases indicates that the ability of Australian courts to make costs orders against non-parties remains questionable and largely turns on the powers bestowed on each court. However, parties may alternatively be able to ensure payment of costs through an order for security for costs.

3.2[a][ii] Security for Costs and Deeds of Indemnity

The Australian courts have more readily embraced requests for security for costs in situations where a third-party funder is involved. In *Domino's Pizza Enterprises Ltd v. Precision Tracking Pty Ltd (No. 2)*,[59] the Federal Court of Australia accepted an application for security for costs, noting that the respondent did not possess the financial capability to meet an adverse costs order. Importantly, it was noted that the mere existence of a litigation funding agreement was insufficient to guarantee that the respondent would be able to meet a potentially adverse costs order.[60] Rather, relying on earlier authorities,[61] the court considered that the presence of a litigation funder was a factor that militated in favor of the granting of security.[62] Robertson J also noted that an undertaking that the funded party would provide notice if there were any changes pertaining to the litigation funding agreement was inadequate to protect the claimant.[63] Therefore, in contexts where the funded parties' financial capacity is limited and litigation funding is employed, it appears that Australian courts will often require security for costs.

However, where security for costs is required, Australian courts have also indicated that a deed of indemnity from a non-party to the proceedings may be acceptable so long as it achieves its purpose as security.[64] In *Australian Property Custodian Holdings Ltd (In Liquidation) v. Pitcher Partners (a firm) and Ors*,[65] the Victorian Supreme Court held that a deed of indemnity from an insurer based

58 *Ibid*. at [34] (Mason CJ and Deane J).
59 [2017] FCA 211 (hereinafter "*Domino's Pizza*").
60 *Ibid*. at [74]–[75] (Robertson J).
61 *Austcorp Project Number 20 Pty Ltd v. LM Investment Management (in Liq)* [2014] FCA 1371, [34] (Gleeson J) citing *Green v. CGU Insurance Ltd* [2008] NSWCA 148, [51]–[53], [82]–[88] (Hodgson JA, with Campbell JA agreeing).
62 *Domino's Pizza*, [75] (Robertson J).
63 *Ibid*. at [74]–[75] (Robertson J).
64 *Australian Property Custodian Holdings Ltd (In Liquidation) v. Pitcher Partners (a firm) and Ors* [2015] VSC 513, [56]–[57] (Lerodiaconou AsJ).
65 [2015] VSC 513.

overseas would be sufficient security for costs. This decision was reinforced by *DIF III Global Co-Investment Fund LP and Anor v. BBLP LLC and Ors* (2015)("*DIF III*"),[66] which, despite finding against the plaintiffs, found that in particular circumstances a deed of indemnity would be adequate security for costs. In *DIF III* Lansdowne AsJ noted that evidence provided by counsel as to the creditworthiness of the third party was insufficient and therefore direct evidence would be required from the organization providing security.[67] Thus, it is likely that Australian courts will be comfortable with allowing litigation funders to provide a deed of indemnity as security for costs. This approach presents litigation funders with a convenient way of meeting security for costs obligations without requiring them to immediately commit capital or provide further guarantees.

3.2[b] International Approaches

International courts have been willing to require a third party to pay costs where a claim fails. As the ICCA-Queen Mary Report highlights, courts in both England and the United States allow costs orders to be rendered against non-parties where they have gained a "sufficient degree of economic interest and control in relation to the claim."[68] As with the Australian approach, these courts also often allow security for costs in appropriate circumstances involving a litigation funder.

3.2[b][i] England

In England, there is a body of well-established case law according to which adverse costs orders may be rendered against non-parties to the litigation.[69] In the English High Court and Court of Appeal this power is underpinned by the Senior Courts Act 1981 (UK), which grants the court the "full power to determine by whom and to what extent the costs are to be paid."[70]

This broad discretion facilitated the decision of the English Court of Appeal in *Excalibur Ventures LLC v. Texas Keystone Inc. and Ors* ("*Excalibur*"),[71] where a third-party funder was ordered to pay costs on an indemnity basis owing to the serious deficiencies in the claimant's conduct of that litigation. While the funders attempted to argue that they had engaged in no "discreditable conduct"[72] and so

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66 *Ibid.* at 484.

67 *Ibid.* at [61] (Lansdowne AsJ).

68 ICCA-Queen Mary Report at 161.

69 *Legg v. Sterte Garage Ltd* [2016] EWCA Civ 97; *Deutsche Bank A.G. v. Sebastian Holdings Inc and Anor* [2016] EWCA Civ 23.

70 *Senior Courts Act 1981* (UK) s. 51(3).

71 [2016] EWCA Civ 1144.

72 *Ibid.* at [23] (Tomlinson LJ).

should not be obliged to pay costs on an indemnity basis, the court found that this ignored their true involvement in the case, through which the third-party funders stood to gain financially as much as the funded parties. Thus, the court found that the third-party funders were unable to separate themselves from the conduct of the litigation and should pay costs on an indemnity basis. *Excalibur* epitomizes the English understanding that often the relationship between the claimant and the third-party funder will justify costs orders against that funder.

Nevertheless, third-party funders have received some protection in English case law. Under the so-called "*Arkin* cap," recovery of costs against third-party funders is limited to the extent of their financial contribution.[73] This cap has received significant criticism in England, as "unduly favouring" third-party funders and support of its legitimacy has begun to erode. This criticism was ventilated in a 2009 report by Lord Justice Jackson quoting the following words of the City of London Law Society's Litigation Committee:

> We consider that the court should have the ability to order the third party funder in an unsuccessful case to pay all of the successful defendant's costs (subject to assessment in the usual way) and its ability to do so should not be circumscribed by the principle in *Arkin*.[74]

Lord Justice Jackson considered it wrong in principle that a third-party funder should be able to avoid a portion of costs in the event of an unsuccessful claim, potentially leaving both the other party and the claimant exposed to additional costs.[75] His Lordship also particularly noted that no such law exists in Australia and that this did not appear to have suppressed the Australian third-party market or had any ramifications on potential access to justice.[76] These criticisms have begun to permeate into English case law. In *Bailey and Ors v. GlaxoSmithKline UK Ltd*,[77] Foskett J provided a significant contribution to this erosion, finding that the *Arkin* cap does not apply in ordering security for costs and somewhat ominously foreshadowed that "a wholesale attack on the reasoning in *Arkin* might be launched."[78] Thus, while the *Arkin* cap presents third-party funders with some protection, its longevity is questionable.

The English courts also possess jurisdiction to order security for costs against third-party funders. In *The RBS Rights Issue Litigation*,[79] the English High Court exercised these powers in ordering security for costs against a commercial litigation funder. The court considered that its decision to order such security

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73 *Arkin v. Borchard Lines Ltd (Nos 2 and 3)* [2005] 1 WLR 3055.
74 Lord Justice Jackson, *Review of Civil Litigation Costs: Final Report* 122 (December 2009).
75 *Ibid*. at 123.
76 *Ibid*.
77 [2017] EWHC 3195.
78 *Ibid*. at [59] (Foskett J).
79 [2017] EWHC 1217 (Ch).

could be informed by the risk of non-payment by the party, some causal linkage between funding and recovery of costs, the motivation of the third-party funder, whether the non-party was aware of the risks of providing funding, and whether there were factors like delay that were relevant.[80] As with the Australian approach, the English courts have also allowed, in appropriate circumstances, a deed of indemnity from a non-party to serve as a security for cost.[81]

The English approach therefore provides for multiple mechanisms through which a non-party will be required to meet potential adverse costs orders.

3.2[b][ii] United States of America

In the United States the question of whether costs can be ordered directly against a litigation funder has received only limited attention. This question is also of lesser significance as the United States does not subscribe to a "costs follow the event" principle but rather generally requires each side to bear their own costs.

However, in *Mohammed Abu-Ghazaleh v. Gerard Martin Demerutis et al.* ("*Mohammed Abu-Ghazaleh*"),[82] the Florida District Court of Appeal made a costs order for attorneys' fees and costs against two litigation funders that had funded the claimant's action. In that case it was noted that these litigation funders had exercised significant levels of control in the litigation, selecting attorneys, recruiting fact and expert witnesses, and were even empowered to veto any proposed settlements.[83] The court therefore considered that their status rose to the level of a party in the proceeding, despite their not being named.[84] *Mohammad Abu-Ghazaleh* illustrates that United States courts may order costs against litigation funders in circumstances where their level of control over the proceedings is such that they could be considered to be an involved party.

3.2[c] Applying these Approaches to Arbitration

As previously noted, the consensual nature of arbitration means that tribunals are often limited in their ability to order costs against non-parties. However, in submissions received by the Hong Kong Law Reform Commission a significant number of respondents indicated their preference that tribunals should be able to take steps to enforce costs awards against third-party funders, "in appropriate

80 *Ibid.*
81 *See Recovery Partners GB v. Rukhadze* [2018] EWHC 95 (Comm).
82 Florida Third District Court of Appeal, Nos. 3D07-3128, 3D07-3130, December 2, 2009, 36 So. 3d 691.
83 *Ibid.*
84 *Ibid.*

circumstances."[85] It has been noted that such a course of action would ensure that parties are not exposed to unpaid costs orders and that third-party funders would only support claims they consider to be of significant merit.[86] The ICCA-Queen Mary Report further recommends that this question should be addressed in institutional or national arbitration rules.[87] Indeed, this position was seemingly embraced by the Draft SIAC Investment Arbitration Rules in 2016, which stated that:[88]

> The Tribunal shall have the authority to order in its award that all or part of the legal or other costs of a party be paid by another party or*, where appropriate, any third party funder.* [Emphasis added]

However, this explicit extension to third-party funders was removed in the final version of the rules released in 2017.[89] Thus, it appears that the legal justifications for such a course of action remain to be seen and so the more likely approach to ensuring costs orders against third-party funders is for the tribunal to require security for costs.

Many common law jurisdictions and several institutions empower tribunals to order security for costs against a party in the arbitration.[90] Generally, arbitral institutions provide for security for costs (e.g., Article 33 of the ACICA Arbitration Rules 2016 allows the tribunal to order security for costs). The International Arbitration Act 1974 similarly empowers tribunals to require security for costs.[91] It therefore appears that for the foreseeable future the Australian approach to the involvement of third-party funding in international arbitration will be to allow tribunals to protect parties through requiring security for costs.

4 CONCLUSION

The Australian experience may inform the approach to third-party funding in international arbitration. However, while it is renowned as a developed jurisdiction for third-party funding, the Australian framework is still undergoing significant evolution and development and so it will be some time before its regulatory frameworks fully mature. Further, issues of disclosure, confidentiality, costs orders, and security for costs, illustrate the challenges posed by the advent of third-party

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85 ICCA-Queen Mary Report at 162; Law Reform Commission of Hong Kong Third Party Funding for Arbitration Sub-Committee, *Third Party Funding for Arbitration* 106 (Consultation Paper, October 2015).

86 ICCA-Queen Mary Report at 163.

87 *Ibid*.

88 *Draft SIAC Investment Arbitration Rules 2016*, r. 34.

89 *SIAC Investment Arbitration Rules 2017*, r. 34.

90 *Arbitration Act 1996* (UK), s. 38.

91 *International Arbitration Act 1974* (Cth), s. 23K.

funding in international arbitration. As the ICCA-Queen Mary Report eloquently observes, "[t]he 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."[92] It seems that further close attention and scrutiny is now required to ensure that the scales are appropriately balanced.

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92 ICCA-Queen Mary Report at 17.