Kluwer Arbitration Blog

Third Party Funding in Sweden – Uncovering Uncharted Territory

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Introduction

Despite a rapid emergence at a global stage, third-party funding (TPF) appears yet as unfamiliar to businesses in the Nordic region. According to a survey included in the 2018 edition of the Roschier Disputes Index, merely 5 per cent of the Nordic companies have used TPF for financing litigation or enforcement proceedings. Arguably, these results mirror that the occurrences of TPF in Sweden have so far been limited to international arbitrations seated in Sweden, i.e. there is no internal market for TPF. Nonetheless, respondents of the survey who had used TPF described positive experiences, which indicates that an increasing number of businesses in the Nordic region will eventually embrace that resorting to TPF for financing arbitration costs is not only possible but may also be viable and beneficial. Concurrently, the already considerable amount of funded arbitrations seated in Sweden will likely increase and attract greater interest going forward.

Alongside the utilities of TPF are several important legal issues. In April this year, the ICCA-Queen Mary Task Force published its Report for public discussion on some of the most pressing of such inquiries, several of which remain yet to be examined from a Swedish viewpoint. As of today, there are no laws or mandatory rules in Sweden regulating TPF and, given the absence of a domestic market, it is unlikely that legislature will be introduced in the near future. Nonetheless, the particular features of Swedish law may have inferences on TPF in international arbitrations seated in Sweden as well as on the prospective emergence of a domestic funding market. This will be dealt with further below.

Restrictions on Risk Arrangements

In Sweden, the structuring of the funding agreement (i.e. the contractual arrangement stipulating the terms behind the funding) is not subject to any common practice. However, the Swedish Bar Association's Code of Professional Conduct (CPC) governs the financial interests of Swedish lawyers. Save upon a set of exceptional grounds, the CPC prohibits lawyers from executing "risk agreements", under which the reimbursement constitutes a percentage of the amount recovered by the client. As TPF will likely remain unregulated, the Bar Association's stringent rules on risk agreements likely do not reflect an impending Swedish approach imposing comparable restrictions towards funding agreements. However, funders, who engage Swedish counsel, must do so accepting that Swedish lawyers utilize traditional fee models. This, in turn, might carry implications to the construction and terms behind the funding arrangement, as some funders are inclined to demand the funded party's legal counsel to part risk through the use of outcome-based fee arrangements.[1)]

Disclosure

The well-articulated issues of disclosure in relation to TPF are strongly linked to the fundamental requirement for an impartial and independent tribunal. The prevailing controversy relates to how the arbitral tribunal can ensure its independence if not informed of the existence of TPF. Currently, neither Swedish arbitration legislation nor any arbitration rules impose any apparent obligation for parties to disclose funding *sua sponte*.

The Queen Mary Task Force Report expresses a stricter view on disclosure obligations than tribunals have tended to do in practice. Among other things, the report suggests that parties "should, on their own initiative, disclose the existence of a third-party funding arrangement and the identity of the funder to the arbitrators".[2)] The IBA Guidelines on Conflicts of Interest expresses an analogous approach. The explanatory section re General Standard 6 (b) states that "[t]hird-party funders and insurers in relation to the dispute may have a direct economic interest in the award, and as such may be considered to be the equivalent of a party", in effect suggesting that the same disclosure requirements that apply to the parties may be imposed towards funders.

It remains to be seen how courts and tribunals in Sweden will handle the correlation between disclosure and TPF. Previously, transnational soft law sources, such as the IBA Guidelines, have influenced the Swedish Supreme Court's interpretation of the provisions relating to conflicts of interest in the Swedish Arbitration Act on several occasions (*See*, e.g., NJA 2007 p. 841 & NJA 2010 p. 317). If applied in a TPF context, this tendency may predict a shifting towards a stricter view on disclosure duties, at least with respect to the existence of funding and the identity of the funder.

Costs

In the Swedish context, case-law has developed regarding investors attempting to attribute the risk for adverse costs liability to shell companies acquired for the sole purpose of pursuing legal claims. In several cases, the Swedish Supreme court has deemed the shareholders of such "claims vehicles" personally liable for adverse costs (See, e.g., NJA 2014 p. 877 and on NJA 2006 p. 420). This veil-piercing doctrine entails that personal liability may step in where the third-party investor has acted as the effective beneficiary in the dispute and where the claim has been transferred to a company in poor financial condition. Furthermore, the cases suggest that personal liability requires that the purpose behind using the claims vehicle is to indemnify the investors in case of an adverse judgment so as to limit the adverse financial consequences of a negative outcome in the dispute. Through this development, the Swedish Supreme Court has sought to prevent arrangements whereby a creditor transfers a claim to a financially weak party in order to discharge the liability for legal fees and litigation costs in the event of an unsuccessful outcome while simultaneously retaining the financial interest linked to a successful outcome.[3)]

In relation to TPF, a discussed issue relates to the notion that funders, in general, do not cover adverse costs. It is debatable whether the view of the Swedish Supreme Court on costs allocation may be applied also to third-party funding in the context of arbitration. If so, does this mean that a third party funder may be ordered to pay adverse costs, for instance through tribunal-ordered costs orders directed towards the funder? We believe that the answer is no, as third-party funding generally does not involve any transfer of claims, i.e. funders do not become formal parties to the arbitrations in which they are invested.

Another measure that could mitigate the risks associated with financially weak parties who opted for the external funding of arbitration claims is security for costs. However, the use of security for costs in arbitrations involving TPF has triggered a heated debate after the tribunal in *RSM v. Saint Lucia*, in a fairly controversial manner, ordered security for costs against the funded claimant. Subsequent to *RSM v. Saint* Lucia, assessments of tribunals provide a multi-faceted view on how to evaluate the relation between impecuniousness and the existence of funding on the one hand, and the general standards for granting security for costs on the other.[4)] As per the latest revision in 2017, the SCC Arbitration Rules contain a provision (article 38) specifically on security for costs. By providing detailed and explicit requisites, including an elucidation that security for costs should be granted only under “exceptional circumstances”, article 38 provides some clarity with respect to the general conditions for granting security for costs. However, as a corollary to the lack of consistency demonstrated in international practice, it is fair to say that a prediction of how tribunals seated in Sweden will apply these conditions with respect to the involvement of a third party funder, is clouded by uncertainty.

The ICCA Queen Mary Task Force report has attempted to mitigate these uncertainties by providing recommendations as to the appropriate standards for assessing security for costs in relation to TPF. From this time and on, it will be interesting to observe what impact these directions will have on how tribunals choose to apply article 38 of the SCC Rules in funded arbitrations brought by impecunious parties.

Looking Forward

The Swedish legal community has previously viewed third-party funding with a fair amount of disinclination. However, during the course of the past year, we have witnessed the development of a more optimistic attitude among practitioners and business representatives alike. It appears indisputable that this emerging trend ventures a perspicuous future for TPF in the Nordic region, and Sweden in particular. Nonetheless, the above-discussed issues constitute merely a selection out of multiple procedural queries relating to TPF and its impact on arbitration. In order to secure a well-operating market, these issues ought to be analyzed more scrupulously and simultaneously interconnected with the characteristics of Swedish arbitration law.

References

?1 *See* Jonas von Goeler, Third-Party Funding in International Arbitration and its Impact on Procedure, International Arbitration Law Library, Volume 35 (Kluwer Law International; 2016) p. 33-34.

?2 *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 p. 81.

?3 Johan Sidklev & Carl Persson "Chapter 5 – Sweden" in *Third Party Litigation Law Review*, 1st ed. (2017) p. 146.

?4 See e.g. EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic, ICSID Case No. ARB/14/14. South American Silver Limited v. Bolivia, UNCITRAL, PCA Case No. 2013-15, Procedural Order No. 10 (Jan. 11, 2016), and Caso CPA No. 2016-08 Manuel Garcia Armas v. Venezuela (Procedural Order dated June 20, 2018).

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