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Comment on the Draft Report of the ICCA/ Queen Mary Task Force on Third Party Funding in International Arbitration

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ICCA/Queen Mary Task Force on Third Party Funding
in International Arbitration

Thank you for the opportunity to comment on the Draft Report of the Task Force. The Draft Report clearly represents a great deal of work on the part of the Task Force members, and is certain to be an important contribution to the much-needed public debate and regulatory efforts surrounding third party funding (TPF).

I have been a professor of International Economic Law (IEL) for over twenty years, with a particular interest in structural and institutional questions in trade law, and in the fairness of the global economic system as a whole. My remarks today grow out of these long-standing concerns, and reflect my research on the structural bases of distributive justice and injustice in IEL. Because of the significance of foreign investment today and growing public concerns over investment treaties, I have expanded my research to include investment law. Most recently, I have written on the parallels between the current legitimacy crisis in investment law, and the earlier legitimacy crisis in trade law (see Garcia et al., *Reforming the International Investment Regime: Lessons from International Trade Law*, 18 Oxford Journal of International Economic Law 861 (2015)). The late 20th century legitimacy crisis in trade law signaled/accompanied an important paradigm shift in our understanding of the trade regime, from being simply the international law of inter-state commerce, towards our recognition of it as a key part of global economic governance, responsible for ensuring a fair global economic system for all affected stakeholders. I understand the investment crisis today in the same vein, and this perspective on investment law as fundamentally entwined with ideas of justice and governance informs my remarks today.

In my view, TPF represents a profound challenge to the fairness and legitimacy of the international investment regime, which if not addressed effectively will further compromise not only the public's faith in this system (already undermined), but the viability of the system for states and other stakeholders. The Draft Report, while offering useful recommendations for addressing important ethical and professional issues raised by TPF, almost entirely sidesteps this fundamental, even existential issue. This might suggest to some readers that the *presence* of TPF in ISDS is beyond regulation or review, that there will be no further public consideration or regulatory response except to moderate some of its effects. One can see in the careful wording of Chapter Eight that the Task Force had to contend with strong differences of opinion on this question. Nevertheless, I am concerned that by its omissions and elisions the ISDS portions of the Draft Report will be read more as a ratification of the status quo with respect to TPF, than as the opening contribution to a searching and public-minded regulatory conversation on TPF and investment arbitration that the Draft Report suggests it seeks to be.

The fundamental premise of my view on TPF is that the current BIT-based international investment regime is fundamentally unbalanced in terms of norms and dispute resolution, offering investors a wide range of protections while offering states no meaningful basis for claims or counterclaims. Indeed, Prof. Alessandra Arcuri of Erasmus University (in a paper presented at the Graduate Institute of Geneva's 2017 Annual Conference on WTO Law) recently referred to this unbalance as "The Great Asymmetry" in international investment law. While there may be valid historical reasons for this asymmetry (see, e.g., Garcia, *supra*), and the threat to the viability and security of foreign investment continues to be real, this asymmetry represents today a fundamental flaw in the investment regime from the perspective of both governance and fairness, the two parameters critical to both resolving the current legitimacy crisis and shaping a more effective investment law regime for the 21st century.

TPF is a threat to both governance and fairness because by design it exploits this asymmetry in ways that further undercut the regime's capacity to satisfy even basic norms of governance and fairness. Whatever the risks and merits of TPF in commercial arbitration (which I don't speak to here), TPF within a system as unbalanced as the investment law regime is, to put it bluntly, a disaster. I say this, because given the structure of the investment regime today, TPF cannot but have the effect of further concentrating economic power in the hands of investors, the privileged class of claimants (indeed the only class of claimants) in the current regime, by opening the system to the resources (and priorities) of speculative investment. This is exactly the risk that traditional common law doctrines of maintenance and champerty were designed to mitigate, and reflects (even intensifies) the reasons investment treaties are under such challenge today.

TPF is a threat to governance, because it further amplifies "voice" on the part of a stakeholder whose voice is already the loudest, if not the only, voice officially recognized within the system (other than State Respondents, whose voice is carefully limited by the asymmetric nature of the substantive rules). It is a threat to fairness, because it intensifies the resources available to a privileged claimant, against a responding party with limited substantive rights and no appellate rights, a party that is burdened by competing sovereign budgetary responsibilities to many stakeholders, and holds a monopoly on the taxing power. In other words, TPF in ISDS gives a small class of investors even more resources to prosecute unbalanced claims against a constrained State, claims that in a majority of cases will ultimately be paid by a large underrepresented class of stakeholders (the public, who as tax payers are the "residual risk-bearers" in the current system). They will pay in the form of additional fiscal or welfare burdens, since both losses and settlements are equally burdensome on the public fisc.

Such imbalances are what international economic law should seek to redress, not facilitate. Business actors will continually seek to concentrate both control and profit while transferring risk, and the task of economic law is to identify such patterns in every transaction and ensure that an appropriate share of risk always remains with those exercising control and receiving the profits (see, e.g., the work of Prof. Joseph Vining). When the law fails to do this, society as a whole suffers, as we saw most recently in the Global Financial Crisis. Here too there are instructive parallels: the crisis grew out of a decision to allow speculative investment into the mortgage lending industry, an industry designed (albeit imperfectly) to balance the social goals of home ownership against the risks of default and the need for a sustainable rate of return, within a framework of prudential regulation. On a structural level, the decision to allow TPF into ISDS functions along the same lines, facilitating the exploitation of the tax-paying public for the benefit of speculative investment.

For these reasons, I would recommend that TPF be barred from all ISDS cases until the system is fundamentally reformed both substantively and procedurally. At a minimum, ordering mandatory security for costs when a claimant is TPF funded, as Dr. Gavan Griffith, Q.C. has advocated in *RSM v. St. Lucia*, would go some way towards addressing this imbalance. Simple disclosure is not, in my view, an adequate remedy when the structural defects of the system are so basic and so prone to exploitation. Allowing TPF to operate unchecked within ISDS reduces an institution designed to address injustice (albeit imperfectly) and maintain order, into a mere speculative investment opportunity, which is precisely what traditional prohibitions on maintenance and champerty were designed to prevent. Certainly it is a step in the right direction to know who is exploiting Arcuri's Great Asymmetry and for whose benefit, but in light of the fundamental inequities described above, it cannot be considered an adequate response.

Although Chapter Eight implies that within the Task Force there would not be majority support for recommending such a ban, or even mentioning it, the failure to more forthrightly address this issue represents a lost opportunity. By taking up an issue with such financial momentum and potential risk without making any concrete recommendations or even directly addressing this dynamic, Chapter Eight as written risks being read as complicit in this and against the public good. TPF in ISDS does not exist in isolation from the Great Asymmetry, indeed, it appears designed to exploit the Great Asymmetry for speculative gain, and the public's best interests are not served by drafting a report that reads as if it did.

Even a more frank discussion of the interaction between the structural characteristics of the contemporary BIT system and TPF as a funding mechanism would go a long way towards bolstering the legitimacy and credibility of this part of the Draft Report, and indeed would embody the commitment to disclosure that the Task Force recommends. Even mentioning the systemic risks and the option of a ban—even if balanced by competing recommendations—for the public's consideration, would allow the Task Force to more effectively achieve its stated goal of contributing to this larger public debate, and help build the more robust and sustainable international investment regime that we all need.