

Three's a crowd? Third-party arbitration funding

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Third-party arbitration funding can benefit both under-resourced growing businesses as well as established and profitable companies, allowing them to cover the legal costs of potentially complex proceedings. However, companies should be aware of its potential risks and downsides, such as concerns over confidentiality and privilege of sensitive information, the funder's self-interest in returning a profit on its investment and potential conflicts of interest between funders and arbitrators. A number of jurisdictions and arbitration institutions are considering introducing external regulation of third-party arbitration funding.

Is third-party arbitration funding common in your jurisdiction?

Third-party arbitration funding has not yet become popular in Poland, but its growing importance in the field of international arbitral practice means that it is gradually entering the Polish market. In particular, foreign sponsors are willing to cover a party's legal fees and expenses incurred in arbitration, as the Polish market is still developing and such investment is needed. As one of the main dispute resolution methods, arbitration is generally not widely used, mainly due to the costs involved, which the parties often cannot cover. Securing external funding may contribute to popularising arbitration, which would result in the increased demand for the funders' services. Funders may operate in specialised fields, such as insurers, investment banks and hedge funds.

What terms and conditions are generally associated with third-party arbitration funding in your jurisdiction? Does this type of funding usually include punitive measures in the event of an adverse outcome for the claimant company?

Polish law does not set out specific rules regarding third-party arbitration funding, but it is allowed under freedom of contract rules. Funders and parties may determine their legal relationship at their own discretion within the general limits of the freedom of contract set out by Polish law. These limits follow the nature of a contractual relationship, good customs and the provisions of law. Further, third-party funding is permissible provided that it does not compromise the integrity of the arbitration proceedings (eg, the arbitrators' impartiality and independence). In Poland, the funding of costs by a third-party may infringe one of the main principles of arbitration (ie, impartiality). This kind of risk may also occur in different circumstances without the funder's involvement. The transparency of proceedings is essential in a situation in which the third party's identity is not disclosed to other participants and it is impossible to analyse the direct or indirect relationship between the arbitrator and the party that has a direct economic interest in the award to be rendered in the arbitration. It appears that full disclosure of the funding terms in arbitration is not required to preserve transparency and mutual trust.

Third-party arbitration funding can involve potential risks for claimant companies. What measures can be taken to avoid or minimise such risks?

The funding of one party's arbitration costs may mean that the other party will be unable to meet an adverse costs award. This, in turn, will often prompt an application for securing the costs. In Polish arbitration proceedings, arbitrators consider third-party arbitration funding to be a relevant factor by arbitrators in deciding on securing the costs. Further, a claimant that enters into an agreement with an investor should consider the circumstances that would result in its liability for the arbitration costs. It is important to avoid a situation in which a significant proportion of the amount

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that the claimant would recover from its opponent would be paid to the funder. Moreover, the costs of packaging and presenting a case to a funder in order to obtain financial support, and any associated negotiations, are generally not recoverable from the funder. The claimant should also be aware of this fact. Despite the fact that the funder is not a party to the dispute and is generally prohibited from controlling the arbitration process, it will probably have an impact on how the case is conducted – in particular, decisions concerning settlement due to the funder's economic interest.

Conversely, an investor often guarantees access to justice for parties that are financially incapable of bearing the costs of arbitration proceedings and would like to obtain a binding verdict.

How does third-party funding affect the confidentiality and privilege of sensitive material in arbitration proceedings?

Entities that provide third-party funding are not included under the arbitration rules. However, funders generally want to be provided with information about the dispute or participate in settlement discussions, where sensitive data could be revealed, such as information regarding the assessment of the dispute. This may cause problems regarding confidentiality and privilege in arbitration proceedings. For this reason, under Polish law, a non-disclosure agreement must be concluded between the parties or their lawyers and the funders. The agreement may also include contractual penalties in the case of a breach of confidentiality. Concluding such an agreement seems to be a rational measure, as there is no legal provision regulating the confidentiality of arbitration in Poland, although it is generally assumed that arbitration proceedings will be private and confidential. The communication between parties or their lawyers and funders is not privileged. However, the non-disclosure agreement does not discharge the parties from the duty to reveal information to authorised public bodies if the disclosure of information is mandatory by law. The breach of confidentiality established by such an agreement may be deemed a criminal offence pursuant to Polish law in certain circumstances. Further, information covered by a non-disclosure agreement may be used in court as evidence.

Given the significant legal and ethical issues associated with third-party arbitration funding, such as potential conflicts of interest and questions regarding impartiality, is external regulation needed in your jurisdiction?

The most relevant issue connected with third-party arbitration funding appears to be regulation, which aims to secure the confidentiality and privilege of sensitive data revealed during the arbitration proceedings or when the investor examines the strengths and weaknesses of the case. Regulation should not only focus on the problem of disclosure of information relevant for the dispute, but also on the issue of revealing the funder's identity to the arbitrators and the non-funded party, which is essential for the integrity of the arbitral system. This is needed to determine the funder's scope of influence and to protect against its undue influence over an arbitration by, for example, reserving the right of approval of the settlement. Further, it is important to regulate the investor's liability for the costs in arbitration proceedings, including:

- legal costs (legal fees and expenses);
- administrative costs (arbitrators fees and arbitration centre costs);
- advisers' costs (expert opinions, valuation reports and technical reports); or
- the method of evaluating the investor funder's return to be tailored to the particular case.

Third-party arbitration funding is still new to the Polish market and regulation is not necessary as yet. The regulations suggested above should be incorporated into the arbitration courts' rules. This would help to define what kind of guidelines will be most required in the practical use of this institution.

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