

Submission on Third-Party Funding

2 September 2021

Submission to UNCITRAL Working Group III on ISDS Reform, contributed by the Columbia Center on Sustainable Investment (CCSI), the International Institute for Sustainable Development (IISD), and the International Institute for Environment and Development (IIED).

I General comments

1. As a key element of the “financial engine” of ISDS, third-party funding is a particularly important reform issue. Several delegations have voiced significant concerns about third-party funding, which highlights the need for deep reform in this area. We commend the Secretariat for the research and work that has gone into the Draft Provisions and encourage the Working Group to continue exploring bold and crucial reform options.
2. Third-party funding links closely to other reform issues identified by the Working Group. There may be a relation between the rise of third-party funding, actual and perceived conflicts of interests, the significant costs of arbitration, and the high amounts of damages claimed or awarded.¹ Additionally, the number and nature of claims, and large damages sought and ordered, relate to other key issues of concern the Working Group has committed to address, such as regulatory chill. Any reforms of third-party funding should thus take a holistic approach that addresses the diverse financial dimensions of ISDS, and the incentives created by third-party funding, in an integrated way. This will help ensure reform of third-party funding mitigates, and does not entrench or exacerbate, other identified concerns about ISDS.
3. In order to ensure that regulation of third-party funding is tailored to effectively address concerns, it would be important to, at the outset of discussion, further articulate the policy aims to be achieved. This can, in turn, more effectively enable the Working Group to distinguish between different types of funding, identify the concerns different types of funding raise, evaluate different regulatory approaches that may be desirable based on the relevant type of funding at issue, and craft clear and workable provisions.

¹ Third-party funders have incentives to ask for large damage awards. A recent study found that as the amount in dispute increases, so do the costs incurred by the disputing parties. See, e.g., Matthew Hodgson, Yarik Kryvoi, and Daniel Hrcka, 2021 Empirical Study: Costs, Damages and Duration in Investor-State Arbitration (BIICL and Allen & Overy, 2021) 26.

4. Relatedly, in order to achieve identified aims, delegates may wish to consider ways that the Draft Provisions and “models” could be combined. For example, states could conceivably combine a broad transparency provision (e.g. *Draft Provision 7*) with a more narrow restriction (e.g. *Draft Provision 5*), and then additionally decide to permit some kinds of funding that would be restricted by adding to these an additional carve-in (e.g. *Draft Provisions 3 and/or 4*). In order to craft a “package” of provisions best suited to address articulated concerns, it would be helpful to further elaborate in the beginning of the paper on the possible components of a regulation, and how those components can be tailored and combined to address different issues raised by different types of funding.

II Specific comments

5. As organisations committed to advancing sustainable development, we commend the Secretariat for considering how issues such as access to justice and sustainable development can be integrated in ISDS reform. However, we have both conceptual and practical concerns about the ways in which the Draft Provisions address these issues. We also have concerns about the possible sanctions outlined in the Draft Provisions. These issues are discussed briefly below, and further addressed in our specific comments to the text.
6. **Sustainable Development.** *Draft Provision 4* suggests permitting TPF for investors that can establish compliance with certain, as yet unidentified, sustainable development provisions. We are uncertain of the rationale for such an approach permitting TPF for these claimants. More specifically, concerns about third-party funding are that it introduces dysfunctionalities that can distort dispute settlement processes and outcomes. Such dysfunctionalities and distortions in the dispute settlement process and law will exist irrespective of whether the investment itself complies with sustainable development objectives. Therefore, it is unclear why such dysfunctionalities and distortions should be permitted simply because the investment seeking such funding complies with certain sustainable development norms. Additionally, this seems to imply that investments that do not comply with sustainable development objectives are and should be entitled to invoke ISDS privileges (though not third-party funding).
7. **Access to Justice.** *Draft Provision 3* suggests that claimants should be permitted to use third-party funding if such funding is necessary to bring the ISDS claim. It is labeled as an “access to justice” model. We would, however, question whether third-party funding can be framed in, and justified based on, “access to justice” terms. For one, there is inconclusive evidence that third-party funding does facilitate access to ISDS for genuinely small and medium-scale enterprises (SMEs), as the amount of SMEs’ claims may not be large enough to attract third-party funding. Additionally, it is important to distinguish between access to ISDS and access to justice. Access to justice can be secured and, for most stakeholders, must be secured, without recourse to ISDS. Investors often turn to ISDS without pursuing other avenues, for example

under domestic law, and without demonstrating that pursuing relief through domestic processes would be futile. But that does not mean that those other avenues are unavailable, or that investors would be without justice if they were unable to pursue ISDS proceedings. The concept of “access to justice” should not have a separate meaning for covered investors (i.e., access to justice equals access to ISDS) than it has for other stakeholders.

8. **Implementation.** Several proposed approaches in the Draft Provisions seem likely to face implementation difficulties. For example, the reference in *Draft Provision 3* to the claimant not being “in a position to pursue its claim without third-party funding” begs questions about how this condition would be assessed (e.g. burden of proof, availability of alternative but more costly financing options, existence of alternative dispute settlement fora). Further, the reference to “investment in compliance with sustainable development requirements” will be difficult to meaningfully implement in practice. Indeed, sustainable development is a broad concept; any references to sustainable development would need to be accompanied by explicit links to international instruments that are formulated in clear, specific language. Additionally, whether an investment advances sustainable development objectives can involve significant argumentation, and there are questions about the financing of costs related to the tribunal’s decision on these issues.
9. **Sanctions.** We note that Sanctions (*Draft Provision 6*) are a critical component of any regulation. We are concerned that some of the current list of proposed sanctions in the draft text (*Draft Provisions 6 and 7*), and the discretion given to tribunals to choose from among the options, may not effectively deter funders and claimants from breaching or seeking to circumvent the rules. The WGIII has identified myriad concerns about TPF that seem to go well beyond those identified by and incorporated into existing treaties (generally limited to conflicts of interest). It would then be appropriate to have sanctions better tailored to this broader set of concerns and not limited to, or even based on, what is in existing treaties. Therefore, we suggest stricter sanctions for violation of regulations intended to address the serious concerns identified by the Working Group III, and requirements on tribunals (e.g. “shall” not “may”). In that regard, we humbly suggest visiting the Section 4 of the CCSI/IISD/IIED 2019 joint submission on [Third Party Rights in Investor-State Dispute Settlement: Options for Reform](#).

III Detailed comments in annex

10. For ease of reference, we have also included comments that are specific to a particular section of the Draft Provisions in track-changes in the enclosed document.