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THIRD-PARTY FUNDING IN CHILE: A REGULATORY PROPOSAL

FINANCIAMIENTO DE LITIGIOS POR TERCEROS: UNA PROPUESTA REGULATORIA

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Abstract

In the last decade, Third-Party Funding has shown a steep rise and has become a consolidated method of providing financial support to pursue a claim. Each country where Third-Party Funding is developing has dealt with this rise in its own way, based on its legal tradition, public policy objectives, and the convenience of letting a new market grow. This article analyses the paths followed by the countries where Third-Party Funding is more developed and proposes a regulatory path for Chile, which takes into consideration the Chilean legal and economic reality and proposes to apply the measures that, in the opinion of the author, have been successful in other jurisdictions.

Keywords: Third-party funding, litigation finance, investment, venture capital, litigation, arbitration, international arbitration.

Resumen

En la última década, el financiamiento de litigios por terceros se ha ido consolidando como método de financiación de disputas legales. Las jurisdicciones más avanzadas en esta materia han enfrentado la nueva realidad desde su propia historia y tradición jurídica, y según sus objetivos de políticas públicas. Este artículo analiza el desarrollo seguido por estas jurisdicciones y formula una propuesta regulatoria para Chile proponiendo, basado en las experiencias más exitosas, medidas ajustadas a la realidad legal y económica local.

Palabras clave: Financiamiento de litigios por terceros, fondos de inversión, inversión, capital de riesgo, litigación, arbitraje, arbitraje internacional.

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1. INTRODUCTION

Third-Party Funding ("TPF") has been defined as "a group of funding methods that rely on funds from the insurance markets or capital markets instead of, or in addition to, a litigant's own funds"[1]. Through a TPF agreement, a firm provides funds to a party to support the costs of pursuing a claim and, in return, receives a share in the outcome or financial charges such as interest.

Litigation financing has grown steeply in the last years, and, in some countries, the market is consolidating at high speed. In the United Kingdom, for example, the litigation finance market total worth is already over 1.5 billion dollars and the number of cases has grown exponentially in the last decade[2]. Similar experiences have happened in other countries such as Australia, Canada, or the United States. The main reasons behind this development are the size of the market and expected returns for investors; in many cases, the returns for firms in litigation finance are "more attractive than equity and fixed-income investments"[3].

The expansion of TPF has brought it to other jurisdictions, among them Chile. Starting approximately a few years ago, when the first incursions of international litigation funds begun, the country has experienced a steady increase of externally funded legal claims. It started with international funds providing financing to mostly international commercial arbitration claims, but it has grown and expanded rapidly. As of today, local firms have emerged offering to fund domestic dispute resolution, and it is expected for more funds to appear and expand their reach within the country.

TPF has several upsides, the most prominent one, its aid to granting access to justice. However, bringing a third-party to a dispute can create several downsides, such as conflicts of interest and ethical struggles for legal counsel. Because of these problems, some criticisms have arisen against it, as of today, its steep growth and the problems it creates have made it one of the most hotly debated topics in litigation[4].

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1 Maya Steinitz, "Whose claim is this anyway? Third Party Litigation Funding", *Minnesota Law Review* 95, n.º 4 (2011), 1,269, 1,275.

2 Justice Not Profit, "Third Party Litigation Funding in The United Kingdom: A Market Analysis", 2015, 1, https://www.justicenotprofit.co.uk/wp-content/uploads/2015/09/Final-TPLF-Paper.pdf.

3 Carol Lewis, "Fancy something different for your Isa? Try a little innovation", *The Times*, 2 March 2019, https://www.thetimes.co.uk/article/fancy-something-different-for-your-isa-try-a-little-innovation-r3b0ms6c5.

4 ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration (International Council for Commercial Arbitration and Queen Mary University of London, 2018), Ch. 1.

This article is divided into three parts. Part 1 will describe the history and development of TPF. Part 2 will analyse the problems it has created in other jurisdictions and the regulations that these jurisdictions have implemented to deal with them. Part 3 will outline propositions of regulatory measures to deal with the effects of TPF in Chile.

2. HISTORIC EVOLUTION OF THIRD-PARTY FUNDING

The use of external support to maintain a claim has a long history, with records of its existence as far back as the ancient Roman times, when to finance a claim in which the financer had no previous interest, made a person liable to an action for *calumnia*. Similarly, Roman Law imposed restrictions on the acquisition of litigious rights either by public officials or average citizens[5]. When the Roman Empire collapsed, many European territories that started to rule themselves independently, adopted Roman Law as the basis of their legal system. With this adoption, the restrictions on maintaining another person's claim were passed on to these newly independent territories.

As centuries passed European legal systems evolved differently in this regard, depending on the legal regime they had adopted. In common law countries, third-party support of claims was prohibited, and several legal doctrines were developed around it. In civil law countries, the regulation inherited to prevent support of third-party claims disappeared with time, but other rules such as the one that regulates the transfer of claims remained.

2.1. Development of TPF on Common Law jurisdictions

For most of the history of the common law, for someone to support a litigious claim in which the supporter had no prior interest, was illegal and a criminal offence[6]. This prohibition can be traced back to ancient times, but it was officially declared in England by the Statute of Westminster, in 1275, that made supporting another person's legal claim a statutory offense[7]. This prohibition was set "to prevent speculation in litigation by those who have no interest in the legal process or the pursuit of justice, and whose activities might amount to an abuse of process"[8].

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5 Max Radin, "Maintenance by Champerty", *California Law Review* 24, n.º 1 (1935), 48-78.

6 Law Commission, Proposals for the Reform of the Law Relating to Maintenance and Champerty (1966), paras 1-8.

7 Statute of Westminster I, 1,275.

8 Christopher Hodges, John Peysner and Angus Nurse, "Litigation Funding: Status and Issues", *Oxford Legal Studies Research Paper* 55 (2012), 12.

The specific conducts prohibited under the common law in this regard were three: maintenance, champerty, and barretry (or barratry)[9]. Maintenance was "the procurement, by direct or indirect financial assistance, of another person to institute, or carry on or defend civil proceedings, without lawful justification"[10]. Champerty was an aggravated form of maintenance, "namely maintenance of an action in consideration of a promise to give to the maintainer a share in the subject-matter or proceeds thereof, if the action succeeds"[11]. Finally, one meaning of barretry was prohibited for these purposes, "the offense of frequently exciting and stirring up quarrels and suits either at law or otherwise"[12]. The modern concept of TPF can fit in either of these conducts.

With the expansion of the British Empire, the common law was exported to new territories. This expansion included, among many other institutions, the doctrines of maintenance, champerty, and barretry, restraining the development of funding of claims as a business opportunity. While maintenance and champerty are present in most common law countries, barretry is less known, but in some jurisdictions such as some states within the United States of America (US), is still in use[13].

2.1.1. The relaxation of the maintenance, champerty and barretry prohibitions

In the last century, for several reasons, many countries started to soften these prohibitions. In many cases, they found that they were no longer necessary because the same objectives sought by these restrictions could be obtained by other institutions. For example, many countries provide free legal aid to the people who can't afford to follow its legal claims in court and have constitutional or fundamental rights, judicially enforceable, that protect people from abuse. Because of these new developments, the prohibitions were falling in disuse. In many countries, champerty or barretry were scarcely applied[14]. Moreover, the prohibitions had some undesired effects. They prevented the growth of firms that could

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9 Lord Neuberger, Harbour Litigation Funding First Annual Lecture, "From Barretry, Maintenance and Champerty to Litigation Funding", Gray's Inn Speech, 2013, https://www.supremecourt.uk/docs/speech-130508.pdf.

10 Chitty on Contracts (28th edition, 1999), paragraphs 17-50.

11 Law Commission, Proposals for the Reform of the Law Relating to Maintenance and Champerty (1966), para 4.

12 Wayne Rhine, "Barratry: A Comparative Analysis of Recent Barratry Statutes", *DePaul Law Review* 14, n.º 1 (1964), 146.

13 Becca Aaronson, "Crackdown intensifies on Barretry", *New York Times*, 23 June 2012, https://www.nytimes.com/2012/06/24/us/crackdown-intensifies-on-barratry.html.

14 N 11, para 7; Maya Steinitz and Abigail C. Fields, "A Model Litigation Finance Contract", *Iowa Law Review* 99, n.º 2 (2014), 725-726.

aid in the promotion of access to justice and limited the alternatives of people to seek alternative methods of dispute resolution.

In consequence, for the relative obsolescence of these prohibitions and for policy reasons, many common law countries decided to lessen the restrictions and allow the growth of TPF. Now, the most common policy reasons behind this decision will be addressed.

2.1.1.1. Access to Justice

Access to justice relates to unmet legal needs. A person may have the legal or even constitutional right to pursue a claim in court but, for lack of resources such as financing, be unable to do it. To deal with this problem, TPF might play a relevant role. Litigation funding facilitates access to the protection of rights in a way that, otherwise, would have been inaccessible for some people or firms[15].

The policy reason behind relaxation revolves around the idea that, by providing funds to support a claim, a person will be able to obtain access to judicial protection and afford legal representation previously inaccessible. Litigation may be expensive and time-consuming, and not everyone who has a legitimate claim can afford to pursue it. In some cases, a person will be able to pursue a claim and seek adequate legal and expert representation only with the support of a financer.

This argument is particularly relevant considering the high costs of pursuing a claim in some jurisdictions. Many of the countries where TPF is most consolidated are also the jurisdictions where is most expensive to litigate a case. In England and Wales, for example, arguably the most consolidated TPF market in Europe, the cost of litigating is the highest in the continent[16]. There, Court of Appeals expressly ruled that allowing TPF promoted access to justice and, in a similar sense, prominent judges and practitioners have defended litigation funding based on equality before the law and access to justice[17].

Another jurisdiction that has followed the same reasoning is Australia. In 1995, Australia started to drastically reduce its expenditure in state legal aid, reaching a 78 percent cut of funds in 2017. This reduction would have limited access to judicial protection of

15 Ylli Dautaj and Bruno Gustafsson, "Access to Justice: Rebalancing the Third-Party Funding Equilibrium in Investment Treaty Arbitration", *Kluwer Arbitration Blog*, 18 November 2017, http://arbitrationblog.kluwerarbitration.com/2017/11/18/access-justice-rebalancing-third-party-funding-equilibrium-investment-treaty-arbitration-2/.

16 Christopher Hodges, Stefan Vogenauer and Magdalena Tulibacka, *The Costs and Funding of Litigation: A Comparative Perspective* (Okford: Hart, 2009), UO Legal Research Paper Series.

17 Arkin v Borchard Lines LTD & ORS [2005] EWHC 2844 Civ 665; N 9, 20.

rights significantly. However, it took countermeasures to control the damaging effects of the contractions of funds. First, removed the ban on contingency fees for legal services. Second, relaxed the prohibitions on maintenance and champerty, allowing "third party commercial litigation funders to flourish"[18]. From a point of view similar to that of the courts of England and Wales, Australian federal courts have expressly declared that the Australian legal framework favours TPF because it improves access to justice[19].

Finally, TPF also enables to balance the playfield between parties with different budgets. Despite the merits of each party's claims and defences, if one of them is capable of spending significant funds things such as legal representation, investigation or expert reports while the other cannot, the first will have better chances of obtaining a favourable decision. TPF could balance the chances of the party in financial disadvantage, providing the funds to find adequate representation.

2.1.1.2. Promotion of Alternative Dispute Resolution Methods

Several jurisdictions have promoted the development of ADRs as a tool to reduce the burden of the judicial system, to enable the parties to settle disputes amicably and economically, and to create areas of business non-existent before its development[20]. These methods are privately financed and promote employment that without ADRs would not exist, such as arbitrators, mediators, and administrative centres. Also, some ADR, like international arbitration, can bring business into a country. When a jurisdiction becomes a regularly required seat for arbitration, several other services such as hotels, restaurants, experts and law firms profit. Also, arbitrators, counsel, and experts of that country are more required and centres that administer international arbitration disputes grow.

In 2017 Singapore and Hong Kong, two of the most prominent arbitration and mediation jurisdictions lifted the prohibitions of maintenance and champerty. They did so only for international arbitration and mediation, to promote these fields. As Singapore's Ministry of Law declared, allowing TPF "will allow international businesses to use the funding tools available to them in other centres and promote Singapore's growth as a leading venue for international arbitration"[21].

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18 N 8, 121.

19 Campbells Cash & Carry Pty Ltd v Fostif Pty Ltd Mobil Oil Australia Pty Ltd, 2005, NSWCA 83 (Australia); Peta Spender, "After Fostif, Lingering Uncertainties and Controversies about litigation Funding", *Journal of Judicial Administration* 18 (2008), 110.

20 Investment Climate Advisory Services of the World Bank Group, "Alternative Dispute Resolution Guidelines", 2011, 7, http://documents1.worldbank.org/curated/en/108381468170047697/pdf/707630ESW0P1160BLIC00153220ADRG0Web.pdf.

21 Public Consultation on the Draft Civil Law (Amendment) Bill 2016 and Civil Law (Third Party Funding) Regulations 2016, para 4 (Singapore).

2.1.2. The current state of TPF in common law countries

As of today, most common law jurisdictions have relaxed the regulations that prevented the development of TPF, but have kept some form of restriction on maintenance, champerty, and barretry. Most countries that lessened the regulations did so only for the situations where the bans were no longer necessary or where TPF does not damage the administration of justice. For example, as explained above, Singapore and Hong Kong allowed TPF only for international mediation and arbitration. England and Wales allow TPF but maintain the prohibitions for situations where the funder has excessive control over the conduct of the claim or where the TPF agreement brings a disproportionate profit for the funder.

However, some countries maintain prohibitions as they have been for centuries. In Ireland, for example, the prohibitions on champerty and maintenance are still in force, and therefore the Irish courts have banned TPF based on these prohibitions. Ireland is the exception among the most developed common law countries[22].

2.2. TPF in Civil Law jurisdictions

Civil law countries have faced litigation funding differently than common law countries. These jurisdictions never had doctrines such as maintenance, champerty, or barretry, so external funding of litigation has never been unlawful. However, these legal systems usually contain restrictions that may affect TPF agreements, making it void or limiting the agreement in a way that makes it financially inviable for the funder.

2.2.1. Limitation to the transfer of litigious rights

The first limitation in civil law countries is the regulation of the transfer of litigious rights. Litigious rights are those credits "which are, or which may be, contested, either in whole or in part, by him whom we pretend to be the debtor of them, whether the process is already commenced, or whether, not being yet commenced, there is ground to apprehend it"[23].

Roman Law set restrictions to the transference of litigious rights that later were adopted by civil law countries[24]. Most of these restrictions, such as the prohibition of public of-

22 Persona Digital Telephony Ltd and another v The Minister for Public Enterprise, Ireland and others, 2017, IESC 27 (Ireland).

23 Robert Joseph Pothier, "Treatise on Contracts (Cushing's Translation 1839)", as cited in Marlin Risinger, "The Transfer of Litigious Rights in Louisiana Civil Law", *Louisiana Law Review* 1, n.º 3 (1939), 596.

24 Risinger, "Transfer...", 596.

ficials of buying litigious rights, were later abandoned by these countries. However, one still survives: the prerogative of the defendant of getting himself released by paying to the transferee the real price of the transfer. Most civil law countries recognise a special prerogative for the defendant in case of the transfer of the litigious right. If a litigious right is transferred, the claimant must notify of this fact to all parties in the proceeding. After this notification, the defendant has the right to pay the transferee of the claim what he paid for the litigious right. If the defendant does so, the transferred litigious right will be extinguished. This prerogative is recognised for example, in the Chilean, French and Spanish civil codes[25].

A TPF agreement is not a transfer of litigious rights, the funder only provides support for the claim, does not acquire it. However, under certain circumstances, if the TPF agreement contains provisions that may lead a judge to conclude that there is an underlying transfer of litigious rights disguised as a TPF agreement, the rules of transfer of litigious rights may apply. In these cases, the defendant will be allowed to pay the funder the money provided to the claimant, and, consequently, obtain the termination of the proceeding and the extinction of the claimant's litigious right.

2.2.2. Maximum interest rate

A second restriction that may apply in civil law countries refers to the interest that legally can be charged for a loan. Many countries set a maximum interest rate that someone can charge to a borrower on a loan. The primary purpose behind this cap, also called the maximum interest ceiling, is "to protect the consumers who cannot afford the high-interest rates offered by formal and informal financial institutions"[26].

Countries have set different consequences for a contract where the interest rate ceiling is surpassed. The most common are two. First, the contract is void. Spanish Law, for example, establishes that if the interest set on a credit agreement is notably superior to the average or that type of contracts or, if in attention to the particular circumstances of a credit agreement it appears as manifestly disproportionate, it will be void[27]. Second, that the interests owed to the lender are reduced. For example, in Chile, the Money Credit Operation Act establishes that a lender cannot charge interest higher than what the Chilean Market Finance Commission (CMF) sets. If a credit agreement exceeds that amount, the interest will be reduced to the conventional interest set by the CMF[28].

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25 *Code Civil*, (France) Art. 1699; *Código Civil* (Spain), Art. 1535; *Código Civil,* (Chile) Art. 1911.

26 Samuel Munzele Maimbo and Claudia Alejandra Henriquez Gallegos, "Interest Rate Caps around the World Still Popular, but a Blunt Instrument", *Policy Research Working Paper* 7,070 (2014), 23.

27 Ley de 23 de julio de 1908, de la Usura (Spain), Article 1.

28 Money Credit Operation, Act 18.010.

These regulations probably will not apply to many TPF agreements. However, if some provisions lead a judge to conclude that the TPF agreement is a credit agreement, they will apply. This can happen, for example, if the TPF agreement sets a fixed return for the funder instead of a share of the outcome of the dispute.

These restrictions also exist in common law countries. However, in common law, they are less likely to apply to TPF. The control of aspects such as the conscionability of the contract and excessive gain of the funder is done by the aspects of maintenance, champerty and barretry that remain in force. These prohibitions are set with similar purposes as the interest cap.

2.3. The current state of Third-Party Funding in civil law countries

In civil law jurisdictions, although there are no express limitations to TPF of a claim, its development has been slower than in common law countries. With few exceptions, in many civil law countries, TPF "is still almost unknown"[29].

Two reasons have been given for this slower development. The first reason refers to the incentives of a party to seek funding. It has been argued that parties have fewer incentives to seek external funding in civil law countries because access to justice is normally free and the costs of litigating a case, such as counsel fees, are relatively inexpensive (compared to some common law jurisdictions). A second reason relates to the incentives of funders, it has been said that the excessive delay in judicial decisions makes civil law markets less attractive[30]. All these reasons have, until now, slowed the growth of TPF. However, this is changing. in several civil law countries, TPF is developing rapidly.

France is one of the civil law countries where TPF has advanced the most. This advancement is mainly due to its position as a world centre for international commercial arbitration. Currently, in French Law, there is no express prohibition of TPF and the main concerns regarding it, refer to possible conflicts of interest. In 2017, the Paris Bar Association issued a resolution supporting TPF, especially in international arbitration, and clarifying, among other things, how the duties of counsel apply to cases where an external funder is present[31].

29 Carmen Alonso Cánovas, "Third-Party Funding: La Financiación Institucional de Litigios y Arbitrajes", *Revista del Club Español del Arbitraje* 9, n.º 9 (2016).

30 Cánovas, "Third-Party Funding".

31 Resolution adopted by the Conseil de l'Ordre (Paris Bar Association) on 21 February 2017 (France).

In Germany and Austria TPF is developed[32]. One funding company has reported examining 10,000 cases since 1998[33]. The TPF market in Germany and Austria has grown as an extension of the legal expense insurance market, highly extended in both countries[34]. Because of this, TPF in Germany and Austria operates under different rules and regulations than most other jurisdictions.

In Latin America TPF has had slower growth. However, in some fields it is already present and increasing its participation. Mainly in international arbitration, where Latin America is rapidly growing and plays an important role. Between 2005 and 2015 the "number of arbitrations seated in Latin America increased by 230%". Also, approximately 29 per cent of ICSID Claims and 15 per cent of ICC claims in 2018 were originated in Latin America[35].

2.4. Third-Party Funding in Chile

TPF has followed in Chile a similar path to most civil law countries. In the Chilean judicial system, claimants unable to adequately defend their claim commonly recur to state aid or lawyers on contingency fees contracts[36]. Chile does not yet have a consolidated funding market and, in many areas of dispute resolution, TPF is unknown. However, there is one field where TPF is rapidly growing in Chile: international arbitration[37]. As in most jurisdictions, international arbitration is where third-party funders aim most of their investments. Among others, the high costs of litigating a case and the high amounts

32 N 16.

33 N 8, 42.

34 N 8, 43.

35 International Chamber of Commerce, Dispute Resolution 2018 Statistics Report (International Chamber of Commerce 2019), 8; International Centre for Settlement of Investment Disputes, 2018 Annual Report (World Bank Group, 2019), 20; Woodsford Litigation Funding, Litigation and Arbitration Funding in Latin America.

36 Elina Meremiskaya, "Financiamiento de Litigios a Través de Terceros y su Aterrizaje en Chile", Centro de Arbitraje y Mediación, Cámara de Comercio de Santiago, 2017, 5, http://www.camsantiago.cl/informativo-online/2017/01/docs/Articulo_Elina.pdf.

37 "El Financiamiento del Arbitraje a través de Terceros desde una perspectiva nacional y comparada", Centro de Arbitraje y Mediación, Cámara de Comercio de Santiago, July 2019, http://www.camsantiago.cl/informativo-online/2019/JUL/news10.html.

of money in dispute on this field make it very attractive for funders[38]. In Investor-State Dispute Settlement (ISDS), for example, there are reports of more than half of investors enquiring about possible funding and the high amount being funded[39].

In Chile, since the beginnings of the twenty-first century, international arbitration has shown a steep growth, aiding the development of TPF. In 2005, following the UNCITRAL Model Law on International Commercial Arbitration, Chile issued the International Commercial Arbitration Act (ICAA)[40]. At that time, international arbitration was not a very developed field, and one of the primary purposes of that act was to promote its expansion and promote the country as a seat of arbitration. As the message of the ICCA put it, the purpose behind it was to position the country as "an arbitration centre in international commerce, particularly, at a Latin American Level"[41].

This purpose, almost 15 years after issuing the ICAA, has to some extent been fulfilled. As of today, many international contracts are setting Santiago, Chile's capital, as the seat of arbitration. The Centre for Arbitration and Mediation of Santiago's Chamber of Commerce (CAM Santiago) has administered more than 3,000 cases between domestic and international arbitration in the last decade and reports an average annual increase in the number cases of approximately 35 percent[42].

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38 David Gaukrodger and Kathryn Gordon , "OECD Working Papers on International Investment, Investor-State Dispute Settlement: A Scoping Paper for the Investment Policy Community", 2012, 19; Jeffery P. Commission, "How Much Does an ICSID Arbitration Cost? A Snapshot of the Last Five Years", *Kluwer Arbitration Blog*, 29 February 2016, http://arbitrationblog.kluwerarbitration.com/2016/02/29/how-much-does-an-icsid-arbitration-cost-a-snapshot-of-the-last-five-years/; Chartered Institute of Arbitrators, "Costs of International Arbitration Survey" CIArb, 2011, 10, https://www.international-arbitration-attorney.com/wp-content/uploads/2017/01/CIArb-Cost-of-International-Arbitration-Survey.pdf.

39 International Council for Commercial Arbitration, "Third-Party Funding", 2017, https://www.arbitration-icca.org/projects/Third_Party_Funding.html; N 4.

40 *Ley de Arbitraje Comercial Internacional* (International Commercial Arbitration Act), Law 19,971.

41 Message from the President to Congress when presenting Law 19,971 of International Commercial Arbitration (Chile); Cristian Conejero Roos, "Análisis comparativo de la influencia de la Ley Modelo de la CNUDMI en Latinoamérica", *Revista Chilena de Derecho* 32 (2006), 89.

42 "Centro de arbitraje más que duplica causas recibidas en tres años", *El Mercurio*, Economía y Negocios, 1 December 2014, http://www.economiaynegocios.cl/noticias/noticias.asp?id=129460; Andrea Chaparro, "48 nuevos árbitros se incorporan al CAM Santiago", *El Mercurio Legal*, 20 December 2013, https://www.elmercurio.com/legal/movil/detalle.aspx?Id=902616&Path=/0D/C5/

This growth is also backed by several reports. A survey of over 500 practitioners done by the University of Leicester and the UK and Gentium Law in Switzerland, showed that almost 15 percent of the respondents recommended Chile among their top five arbitration jurisdictions, making it the highest-ranked jurisdiction in Latin America[43]. Similarly, the International Comparative Legal Guides (ICLG) after analysing ten of the most developed Latin American jurisdictions, concluded that Chile "should be considered as a reputable, reliable and comfortable seat for international commercial arbitration"[44].

A recent reflection of the development of Chile as a centre for arbitration in Latin America is the agreement signed this year between the World Bank, the Ministry of Production, Foreign Trade, Investments and Fisheries of Ecuador and the Centre of Arbitration and Mediation of the Santiago Chamber of Commerce to promote Chile as the seat of investor-state arbitrations in which Ecuador is involved[45].

Through arbitration TPF is entering Chile and, with the growth of this field, more litigation funding firms will enter the market. This increasing number of arbitrations seated in Chile is likely to serve as a beachhead for funders to get into the Chilean market and start providing services in other fields such as class claims or litigation. Chile must start looking at the development of TPF as a close reality and assess the best way of dealing with it. Particularly considering the problems it can create, that will be addressed in the next part of this essay.

3. THE RISKS OF THIRD-PARTY FUNDING

Common law countries decided to relax the prohibitions that limited TPF based on several reasons, one of them was that the problems that these prohibitions addresses are currently being dealt with by other, more efficient, regulations. In this regard they are right, the problems that originally triggered the need for banning TPF today are controlled. Nevertheless, TPF still generates problems, there are issues with TPF that can be highly detrimental to the due administration of justice, and the adequate functioning of the judicial system.

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43 Tony Cole, Pietro Ortolani, Pinar Karacan and Stephanie Trindade Cardoso, "Arbitration in the Americas Survey", University of Leicester and Gentium Law, April 2018, 14, https://www2.le.ac.uk/departments/law/research/arbitration/.

44 Luis O'Nagthen and Jessica Marroquin, *Latin America Overview: A Long Road Travelled; A Long Road to the Journey's End: International Arbitration 2018* (London: ICLG, 2019), Chapter 4.

45 "El CAM Santiago y Ecuador cierran acuerdo jurídico de arbitraje", CAM Santiago, July 2019, http://www.camsantiago.cl/informativo-online/2019/JUL/.

In this part, this essay will discuss two of the most damaging problems generated by TPF. First, how it can affect the independence and impartiality of adjudicators. Second, the undue influence that a funder can exert over the control of the claim[46].

3.1. Conflict of interests of adjudicators

The independence and impartiality of the judiciary are essential components of most legal systems[47]. These requirements are so relevant that they are normally recognised at constitutional legal levels and a judgement rendered by a biased adjudicator can lead to the annulment of a decision or even to criminal prosecution[48].

Most jurisdictions set a system to ensure independence and impartiality. This system is usually designed based on the existence of a dispute where those with an interest in its result are only the claimant and defendant parties. Because of this assumption, most systems analyse the possible conflicts of interest looking only at the claimant and the defendant (and their legal counsel). TPF creates problems because it brings a new entity to the dispute with a direct interest in its result. This new entity can be a cause of bias for an adjudicator, but its outside of the scope of the referred system.

Most legal frameworks do not require parties to disclose the existence of third-party funders, an insufficiency that may risk gravely the independence of adjudicators. Hypothetically, a funding firm can be owned by the adjudicator or the adjudicator may have an emotional predisposition against the funder and, because there is no requirement of disclosing its existence or interest in the dispute, the proceeding can continue and be decided by that judge. Because of this, the threat to the independence of adjudicators is one of the first and stronger criticisms formulated against TPF[49].

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46 In discussions about TPF, there are two other problems recurrently treated: issues with security for costs, and the extent of the attorney client privilege. This essay will not address these two topics. The first issue, because under the Chilean legal framework security for cost does not exist. The cost awarded by tribunals tend to be very low so there are no discussions about the capacity of the claimant to pay them. The second issue, because Chilean Law already provides tools to ensure the protection of professional secrecy in case of TPF.

47 Jeffrey M. Shaman, "The Impartial Judge: Detachment or Passion?", *DePaul Law Review* 45, n.º 605 (1996), 60.

48 Robert M Bloom, "Judicial Integrity: A Call for Its Re-Emergence in the Adjudication of Criminal Cases", *The Journal of Criminal Law and Criminology* 84, n.º2 (1993).

49 N 4, 82.

This problem has been addressed, by different sorts of regulations. For example, the IBA Guidelines on Conflict of Interest in International Arbitration include a duty of disclosure of any relationship "between the arbitrator and any person or entity with a direct economic interest in, or a duty to indemnify a party for, the award to be rendered in the arbitration"[50]. Similarly, the Proposals for Amendment of the ICSID Rules launched by the ICSID Secretariat includes a continuing obligation to disclose the name of any external funder[51].

3.2. Undue influence of the funder over the conduct of the claim

Another of the conflicts that TPF can create refers to the control of the claim. When a TPF agreement is being performed, the funder assumes the costs of the legal counsel, the expert reports, and any other additional expenses. In this context, it is likely for the claimant and the funder to be immersed in an asymmetric relationship where the funder takes the lead and the claimant follows.

The influence of the funder over the conduct of the claim has been the object of debate, some argue in favour and some against it. Those who defend it, do so based on two arguments. First, that it should be admissible because a funder needs to protect its investment. In their opinion, an investor must make sure that the dispute in which invested is adequately conducted and that all the efforts to obtain a favourable award are in place. This argument has been supported, to some degree, by the England and Wales Court of Appeals (EWCA). The EWCA said that a third-party funder's "rigorous analysis of law, facts and witnesses, consideration of proportionality and review at appropriate intervals' is what is to be expected of a responsible funder"[52].

A second argument relates to the expertise of the funder. Those who defend it argue that funders, because of their business knowledge and experience, are experts in dispute resolution. They argue that firms are normally specifically dedicated to funding legal claims and have in their staff lawyers and experts on litigation and arbitration. In their opinion, this expertise makes the influence over the conduct of the claim beneficial for its success[53].

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50 IBA Guidelines on Conflicts of Interest in International Arbitration S.7 (a).

51 Proposals for Amendment of The ICSID Rules, Working Paper 3, Volume 1, English (August 2019), 294.

52 Excalibur Ventures v. Texas Keystone and others [2016] EWCA Civ 1144 1 WLR 2221.

53 Susanna Khouri, Kate Hurford and Clive Bowman, IMF Australia, "Third party funding in international commercial and treaty arbitration – a panacea or a plague? A discussion of the risks and benefits of third-party funding", Bentham IMF, 2012, 5, https://www.benthamimf.com/docs/default-source/default-document-library/573330_1.pdf?sfvrsn=2.

In our opinion, the arguments in favour of the influence over the conduct of the claim referred above are only apparent and the downsides are real and damaging. We are among those against allowing the influence of the claimant over the conduct of the claim.

The arguments in favour of this influence are apparent because with TPF the adequate protection of the funder's investment and the correct conduct of the claim are obtained. The influence of the funder is not needed. As it was referred to in Part 1, one of the main benefits of TPF is that allows the claimant to access the optimum legal counsel, otherwise inaccessible due to budgetary restrictions. Because of TPF, the claimant obtains access to the best legal advice. With this high-quality legal advice, the conduct of the claim is done at the best level possible and the funder's investment is protected. Both upsides referred above are obtained without the aid of the funder.

The downsides, however, are real. The problem that this influence can create and how they can challenge the due administration of justice will be referred below.

3.2.1. Clash of interests between the claimant and the funder

The first perspective from which the influence of the funder over the conduct of the claim creates problems arises because the interests of the claimant and the funder are not always in line[54]. One of the main purposes of the judicial power is the protection of every person's legal rights. The judiciary fulfils this purpose through legal proceedings where anyone can ask for the enforcement of their rights. If an external influence is allowed to intervene and stir a process in a direction that is not the protection of the legal right of a claimant, the judiciary is not fulfilling its purpose. The influence of the funder over the conduct of the claim can lead to this result, particularly when the interests of the funder and the party diverge.

A typical situation where this can happen is when the party faces a settlement proposal. In this case, the interests of the funder and the party can differ. On the one hand, the claimant may be interested in settling the claim, even for a fraction of what is being claimed. This can happen, for example, because the settlement offer includes the design of a new business relationship with the defendant that will be more profitable for the claimant than a favourable judgement. The funder, on the other hand, will not profit from such a settlement proposal, or it will profit considerably less. The interests of the funder lay in the final decision. The larger the damages that decision awards to the claimant the higher will be the profits for the funder, so it will want to pursue the claim to its end.

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54 Susan Lorde Martin, "Litigation Financing: Another Subprime Industry that has a Place in the United States Market", *Villanova Law Review* 53. n.º 1 (2008), 83, 87-90.

In this situation, the interests of the claimant and the funder are in a collision. If the relationship between them is not adequately regulated in the funding agreement, the funder may influence the claim in a direction against the interests of the party, contrary to the due administration of justice.

3.2.2. Ethical conflicts for legal counsel

A second perspective from where this influence creates problems refers to a lawyer's ethical duties. When a lawyer representing a client in court, only the client ought to be the one giving instructions. The client's interests are the ones being defended in the proceeding and counsel should always act in the best interests of its client. The problem arises because some forms of TPF create incentives for counsel to act in the interests of the funder instead of the party.

In a standard situation where TPF is in place, the claimant hires legal counsel and, independently or under the advice of that legal counsel, seeks funding. In these situations, lawyers will be hired directly by the client and will have no duties towards someone else. However, there are some variations of TPF that have arisen in the last years that are starting to blur the line between lawyer, client, and funder. Particularly, Portfolio Funding and Law Firm Funding.

Portfolio Funding is a variation of the standard TPF agreement in which a funder finances several cases instead of just one[55]. Law Firm Funding is a type of Portfolio Funding where a firm funds several cases of a law firm, where the claim holders can be different clients of such a firm[56].

In Law Firm Funding, the members of the law firm are in a situation where their economic interest and their ethical duties conflict. On the one side, the lawyers have ethical duties towards their clients and must represent their interests. On the other side, there is an agreement with the funder from which the lawyer profits in a long-term relationship receiving funds to support several disputes. This situation can be even more conflictive because in some cases where there is not even a contractual relationship between lawyer and client. In some cases, "the portfolio funding agreement is only between the law firm and the funder"[57]. In these cases, the duties of the lawyers are likely to be confused.

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55 N 4, 38.

56 N 4, 38-39.

57 N 4, 38.

This conflict of duties can lead the lawyer to advice the party to take a strategic decision more favourable to the funder than to the person whose interest should be protecting. Following the same example referred above of a settlement proposal received by the party, the lawyer may advice its client to reject it because it is not in the interest of the funder. Even though for the party a settlement would be better than pursuing the dispute, the lawyer has strong incentives to advice against it.

Because TPF can give incentives to lawyers to act against their ethical duties of loyalty to their clients, some countries have regulated it. For example, Hong Kong in its recently issued Code of Practice for Third-Party Funding of Arbitration prohibits funders from taking any steps that "cause or may cause the funded party's legal representative to act in breach of its professional duties"[58]. The Code of Conduct for Litigation Funders of England and Wales also has a similar provision, establishing that a funder will "not seek to influence the Funded Party's solicitor or barrister to cede control or conduct of the dispute to the Funder"[59].

3.3. Regulatory reactions to the problems of third-party funding

As a consequence of the drawbacks that TPF can generate, several jurisdictions have started to take action to regulate it and control its effects. For these purposes, they have taken different regulatory paths. These paths can be grouped in three; (i) the judicial approach; (ii) the self-regulatory approach; and, (iii) the statutory approach. These approaches are can be taken together; most countries have regulated TPF through a combination of them.

3.3.1. The judicial approach

The first of these methods of regulating TPF is the judicial or *ad hoc*. This approach has been mainly taken by common law countries, particularly because of the binding effect that judicial precedent has in their legal framework. In these countries, the courts have maintained the prohibitions of maintenance, champerty, and barretry, and, by judicial decisions, allowed TPF for some situations or under certain circumstances.

Ireland is the country that maintains the most radical judicial regulation of TPF. In Ireland maintenance and champerty are still tortious and criminal offenses, so TPF is not allowed. In 2017, the Supreme Court of Ireland ruled that an agreement to fund a claim is champertous "as described in case law by the High Court and this Court over the last four decades"[60].

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58 Code of Practice for Third-Party Funding of Arbitration (Hong Kong), Section 2.6 (3).

59 Code of Conduct of the Association of Litigation Funders of England and Wales (2011).

60 N 22.

Australia, on the other hand, is one of the most liberal jurisdictions that have followed this approach. The Australian High Court allowed litigation funding based on access to justice reasons and have ruled that TPF is lawful even when the funder maintains some degree of control over the conduct of the proceeding[61]. In Australia also some individual states such as New South Wales and Victoria have allowed TPF through statutes[62]. All this has made Australia one of the countries where the TPF is most consolidated.

England and Wales are situated in between the Irish and the Australian approach. The judiciary, in series of judgements that culminated with the decision in Arkin v. Borchard Lines, has allowed TPF but maintains the prohibition for situations where the TPF agreement contains elements of impropriety such as excessive control of the funder over the conduct of the claim or disproportionate profit[63].

In a way, England and Wales have taken a hybrid regularity strategy and combined the judicial approach with the self-regulatory. In 2011, the Civil Justice Council, an agency of the Ministry of Justice, issued a Code of Conduct for litigation funders. These funders, grouped in the Association of Litigation Funders of England and Wales, are in charge of self-regulating their conduct based following the directions of this code. The code regulates, among other things, duties of disclosure and the influence of the funder over the conduct of the claim[64].

3.3.2. The self-regulatory approach

The second method is self-regulation. One of the most relevant legal jurisdictions that have taken this approach is France. In France there are no maintenance or champerty doctrines and, therefore, TPF is not expressly prohibited (nor expressly allowed). Also, in France judicial decisions are only binding for the parties of the case where the decision is issued. Therefore, TPF can't be regulated by the judiciary.

In 2017, the Paris Bar Council issued a resolution regarding TPF. The resolution declared that TPF is in benefit of both parties and counsel and set ethical obligations for counsel facing claims externally funded[65]. This resolution forbids legal counsel of a party to provide legal advice to the third-party funder of that party. Also, it allows lawyers to meet

61 N 19.

62 Maintenance, Champerty and Barratry Abolition Act 1993 No 88 (New South Wales, Australia); Wrongs Act No. 6420 of 1958, Section 32 (Victoria, Australia).

63 N 17.

64 N 59.

65 N 61.

with the third-party funder only in the presence of their client and sets a duty for lawyers to take instructions only from the party. This resolution also recommends disclosing the existence of funding agreements to the tribunal.

England and Wales, Hong Kong, and Singapore have partially followed this approach, combining the regulation through judicial decisions or statute with self-regulation. The most common method of self-regulation in these countries has been the issuing of codes of conduct for litigation funders and lawyers.

3.3.3. The legislative approach

The third approach is the legislative approach. This method has been taken by two of the jurisdictions where arbitration is more developed in Asia, Singapore, and Hong Kong. Both countries made a legislative decision relaxing the prohibitions on maintenance and champerty for some areas of dispute resolution, opening the door for the development of TPF in those areas.

In 2017, Singapore passed a law abolishing the prohibitions that impeded TPF for some types of dispute resolution, mainly related to international arbitration[66]. Together with partially lifting the prohibitions, Singapore set some regulations to control the drawbacks that TPF can cause. It set provision to control, for example, the relationship between lawyers and funders[67]. Singapore also amended its internal regulations setting a requirement for practitioners to disclose the existence of a TPF agreement and the identity of the funder[68].

Hong Kong followed a similar path. In 2017, passed an amendment of the Arbitration and Mediation Act lifting the prohibitions of maintenance and champerty for arbitration[69]. The amendment also set obligations for parties when a TPF agreement is in place. For example, it requires parties to disclose to the arbitrators and the opposing parties the existence of a TPF agreement and the identity funder. To approach the other problems that arise out of TPF, Hong Kong commissioned a body to issue a code of conduct for funders. The Hong Kong Code of Practice for Third-Party Funding of Arbitration was issued on 7 December 2018 and entered into force on 1 February 2019[70].

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66 Civil Law (Amendment) Act (CLA) No. 2 of 2017 (Singapore).

67 Ibid.

68 Legal Profession Act and Legal Profession Rules (Singapore).

69 Arbitration and Mediation Legislation (Third-Party Funding) (Amendment) Ordinance No 6 2017, A137 (Hong Kong).

70 N 58.

These are the roads that countries have followed to control the harmful effects of TPF. Based on the alternatives that these jurisdictions have laid down, in the following part, this essay will propose a regulatory path for Chile.

4. THE NEED FOR REGULATION OF THIRD-PARTY FUNDING IN CHILE

Common law jurisdictions have faced TPF from a different starting point than where Chile stands today. In the common law, as it was referred to in Part 1, there were prohibitions of providing support to another person's claim aimed to prevent several it created, that prevented the development of TPF. When common law countries decided to allow TPF, they did so by lifting partially the ban on maintenance, champerty, and barretry, and keeping the other part in place. Because of this decision, some of the problems of TPF were controlled by the previous legislation until in place. In civil law, there are no such regulations that can protect citizens, at least partially, from the damaging effects of TPF. In consequence, a special regulation is even more necessary under civil law countries like Chile than common law ones.

4.1. The proposed regulatory path for Chile

The damaging effects of TPF have been controlled through judicial decisions, by promoting self-regulation or by legislation. In Chile, as it will be explained, judicial regulation is not possible, only legislation or self-regulation are viable solutions.

4.1.1. Judicial regulation is inviable under Chilean Law

Chile is a civil law jurisdiction where the law is created and developed solely by the legislative power and where judicial precedent is not binding[71]. The legislative and public policy decisions are to be made by the legislative body, the Chilean Congress, and the role of the judiciary is limited to the interpretation and application of that law. Therefore, regulating through the judiciary is not viable in Chile. The regulation needs to come from somewhere else.

4.1.2. Statutory regulation is the most adequate to the Chilean legal system

Statutory regulation, or legislation, would be an adequate method of controlling in Chile the unwanted effects of TPF, for the following reasons. First, because statutory regulation enhances legal certainty, legislation is binding for all citizens and statutes are of easy and public access. All funders, lawyers and parties participating in a claim filed in a court or tribunal seated in Chile, will be bound by legislation on TPF. The rules regarding their operation will be visibly defined. In consequence, there will be more clarity about where TPF is allowed and what conducts are prohibited for funders, parties, and lawyers.

71 *Código Civil* (Chile), Article 3.

Second, because regulating through legislation allows for a harmonic interaction between the provisions on TPF and the rest of the Chilean legal framework. If the regulation is issued through statute, its provisions will be submitted to the approval of the legislative power and integrated into the Chilean legal framework as a whole. By doing this, the rules of TPF can be harmonised with institutions and rights established in other statutes and prevent legal confrontation or misinterpretations.

If the regulation is produced, for example, by an association that operates in the regulated market, this consistency will be harder to obtain. Groups or associations tend to act in defence of their interests. Considering that the interest of funders is to maximise profits, an association of funders will try to self-regulate as little as possible, or in ways that don't damage its business. The interests of a group will not necessarily be aligned with the due administration of justice or with the defence of constitutional or fundamental rights. Leaving the regulatory decision to them is not likely to serve the public interest in the most satisfactory manner.

4.1.3. Self-regulation as a second alternative

Countries have implemented self-regulation through codes of conduct for associations of funders and lawyers. These codes of conduct are binding for all members of the association that issues them, such as the Association of Litigation Funders in England and Wales and the Paris Bar Association in France. Self-regulation is viable under the Chilean legal framework, several professional and gremial associations include binding codes of conduct for their members. However, as a solution to the problems that Chile faces with the growth of TPF, it would be a weaker response than legislation.

The main weakness of this alternative is that in Chile it is not mandatory to affiliate to an association. Moreover, it is constitutionally forbidden to force someone to integrate them. Historically, it was mandatory for professionals to integrate professional associations and to be bound by their directives, but this situation changed with a series of reforms that were implemented in Chile after the Constitution of 1980[72]. These reforms, applying the freedom of association set in the new constitution, established that no person can be forced to join a group and lifted the mandate to be a member of a professional association[73].

A code of conduct, such as the French or the English would be a viable way of controlling the unwanted effects of TPF in Chile. However, it would be weaker than statutory regulation.

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72 Decreto Ley 2,757, 1981 (Chile); Decreto Ley 3,163, 1981 (Chile).

73 Chilean Library of Congress, La regulación de los Colegios o Asociaciones de Profesionales en Chile y la Legislación Comparada (Report to the Chamber of Representatives), 3-5.

4.2. Proposed regulations to control the undesirable effects of TPF

Having explained why it is necessary to regulate TPF and the alternatives to control it, it's necessary to address what aspects of it ought to be regulated and to what extent. To make a regulatory decision is no simple task, a regulatory measure can have unpredicted effects and cause more damage than it prevents. As John Maynard Keynes famously stated almost a century ago, modern history "offers manifold examples of ill-conceived impediments on freedom which, designed to improve the favourable balance, had in fact a contrary tendency"[74].

Because of this risk, Chile needs to regulate only the aspects of TPF that can cause damage and must regulate them only to the extent that they are prejudicial. The purpose is to prevent the undesired effects of TPF, not to limit the development of the litigation funding market in Chile, that improves access to justice and creates business. This section will outline ideas to counter the undesired effects of TPF from a legal perspective. The same objectives or measures could be adopted by a code of conduct, however, as referred above, it is likely to have a lower impact than statutory regulation.

4.2.1. First regulation: Modernisation of the system to ensure independence and impartiality of adjudicators

The first and arguably most relevant problem that arises out of TPF refers to conflicts of interest in adjudicators. To deal with this problem, Chile needs to adjust the system in place set to ensure the independence and impartiality of adjudicators.

The current system to ensure independence and impartiality. This system is set at two legal levels. First, at a constitutional and human rights level, and second, at a statutory level. The first is the fundamental right to be judged by an independent adjudicator. This right is recognised in the Chilean Constitution as part of the right to a rational and fair proceeding[75]. Also, several international treaties ratified by Chile, such as the American Convention on Human Rights, recognise the right to every person to an "independent, and impartial tribunal"[76].

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74 John Maynard Keynes, *The General Theory of Employment, Interest, and Money* (London: Wordsworth, 2017), 301; Napoleão Casado Filho, 'The Duty of Disclosure and Conflicts of Interest of TPF in Arbitration", *Kluwer Arbitration Blog*, 23 December 2017, http://arbitrationblog.kluwerarbitration.com/2017/12/23/duty-disclosure-conflicts-interest-tpf-arbitration/.

75 *Constitución Política de la República de Chile* (Chilean Constitution), Art. 19 n.° 3; Andrés Bordalí Salamanca, "El derecho fundamental a un tribunal independiente e imparcial en el ordenamiento jurídico chileno", *Revista de Derecho de la Pontificia Universidad Católica de Valparaíso* 33 (2009), 263, ch 1-2.

76 American Convention on Human Rights, Article 8.

The second is the statutory system in place to protect and ensure this right to an independent adjudicator. This system sets a series of grounds for disqualification of an adjudicator and a duty of disclosure. The grounds for disqualification are established by the *Código Orgánico de Tribunales* (COT). This code includes as grounds for challenge, for example, the judge having an interest in the results of the case or the existence of a business relationship between the judge and one of the parties. Chilean Law sets these motives for challenge as *numerus clausus*.

The COT also sets a duty of disclosure[77]. When a judge is under any of the grounds for challenge that the COT establishes, it is under a legal duty to communicate it to the parties. Unlike more modern regulations, this duty is restrictive and applies only to the judge. Parties are under no duty to disclose is they are aware of any of the grounds for challenge[78]. Also, because the grounds for challenge are *numerus clausus*, there is no legal requirement to expose situations that may interfere with the independence or impartiality of the adjudicator but are not included in the grounds for challenge[79].

In the traditional or more typical way of litigating a case, where no TPF is in play, this system, although it has is deficiencies, works relatively well. Everyone that participates or has a direct interest in the results of the dispute appears openly in the proceeding, so the identity of everyone involved in the dispute is of open knowledge. Therefore, any relationship between them can be policed by the parties and, if anyone believes that the independence or impartiality of the adjudicator is at risk, can request its disqualification. However, in a situation of unregulated TPF where an undisclosed third-party with a direct interest in the result of the case exists, this system is insufficient. The current grounds for challenge do not include a relationship between an adjudicator and a third-party funder. And, even more, the claimant is in no obligation to disclose neither the existence of a TPF agreement nor the identity of the funder.

Because of these regulatory deficiencies, a judge could have a bias towards one party because of a relationship with a third-party funder, and the other parties not be aware of it. As of today, a claim in Chile can be financed by a relative of the judge deciding the case, and there is no legal duty for the judge to be disqualified or for the funded party to disclose that fact to the other party. This problem needs to be addressed.

Proposed legal modifications. Chile needs to make two main modifications to this system to ensure the independence and impartiality of adjudicators in disputes where a party is

77 Código Orgánico de Tribunales, Art. 199 (Chile)

78 Leslie W. Abramson, "Judicial Disclosure and Disqualification: The Need for More Guidance", *Justice System Journal* 28, n.º 3 (2007), 301.

79 N 77.

receiving funding from a third-party. First, a redefinition of the grounds for challenge of adjudicators and, second, an ampliation of the duty of disclosure.

Modification of grounds for challenge. The first modification is to redefine the grounds for challenge set by the COT. The current grounds are established in a closed list of specifically defined conducts, relationships, or conditions that create in the adjudicator a bias towards one of the parties. The problem with these grounds is that they are set as *numerus clausus*, and what is not included in the list does not merit disqualification, even if it creates a bias.

The law, to prevent conflicts of interest for unforeseen situations like the ones generated by TPF agreements, should redefine the grounds of disqualification, including a general and basic standard of independence and impartiality of adjudicators. If a party suspects that a specific situation creates a bias, it can challenge the adjudicator, disregarding the specific reasons or facts that lead to that bias. If the one decides on the request for disqualification considers that the facts presented lead to bias, the adjudicator will be disqualified based on this general standard.

After the basic standard of independence and impartiality, the law should include the grounds for challenge that the COT currently recognises as situations that bias adjudicators. The situations described in the grounds for challenge are of those where an adjudicator will hardly remain independent and impartial. For example, if a judge is married to one of the parties or is best friends with the lead counsel of one of the parties, it should not adjudicate that case. These situations should be included as grounds where the law presumes bias in the adjudicator and, when accredited, merit automatic disqualification. However, they should not prevent parties from challenging the adjudicator based on the general standard.

With reform in this direction, new or unforeseen situations capable of affecting the independence of a judge can be addressed. The relationship between a judge and a third-party funder, currently not included among the grounds for challenge, could be considered as bias and merit the disqualification of the judge.

It can be argued that under the current legal system, judges in Chile are already under the abovementioned general standard set by the constitution and the international treaties ratified by Chile. Applying this principle, a judge with a relationship with an entity directly interested in the results of the dispute being judged would violate its constitutional duties.

However, considering that there is a statutory system in place that does not expressly recognise the referred standard as a ground for challenge, the statutory proceeding to obtain the disqualification of the adjudicator could not be used by the parties. Under the current system, to request the enforcement of the constitutional right would have to take

a longer, more complicated, and less efficient road. A modification to the regulation in the COT would make the protection of the constitutional right more certain, efficient, and less costly.

Enhancement of the duty of disclosure. The redefinition of the grounds for challenge, by itself, is not enough to deal with the drawbacks of TPF. A modern and well-functioning disclosure duty is a crucial element to ensure the independence and impartiality of adjudicators. As the ICCA-Queen Mary Task Force Report affirmed, an adequate duty of disclosure "is necessary for an arbitrator to undertake analysis of potential conflict of interests"[80]. Without a modern standard for this duty, the modifications proposed above would not produce the desired effects.

The first reform needed to set an adequate duty of disclosure in Chile is to redefine the obligation set for adjudicators. Under the current regulation, a judge is under the duty to reveal only when considers to be under one of the grounds for challenge that the COT sets. This is problematic because a judge may overlook or decide to ignore some situations that may affect its independence and parties will not be aware of these situations or may find out about them when it is too late.

The duty of disclosure should set an obligation for adjudicators to reveal every situation that may reasonably lead to questioning their independence or impartiality. Once the parties have the information, they can decide whether they want to challenge the adjudicator based on the revealed fact or not.

The second reform is to extend this duty to all parties involved in the dispute. As of today, in Chile, only the judge is under the duty of disclosure. Parties have no duties in this regard. Considering that a TPF agreement is a private contract between a party and a third-party funder, in many cases, only the funded party will be aware of its existence. That party is the only one with access to the information that may risk the independence of the adjudicator. For this reason, the duty of disclosure should be extended to the parties.

A third useful reform would be to make unambiguously clear in the provision that regulates the duty, that it needs to be executed as early as possible in the dispute. Not only because it is more efficient to decide on the subject in an early stage of the proceeding but also to prevent misuses. When the duty of disclosure pends over the parties, if it is not clear that they need to perform it as soon as possible, they may abuse it. For example, a defendant aware of a conflictive situation could delay its disclosure, wait for the passing of time, exercise obtaining the annulment of the proceeding, and delay a final decision.

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80 N 4, 98.

With these reforms to the COT, the Chilean legal system would be able to deal with the conflicts of interest that TPF can create in adjudicators. Moreover, a reform in this sense would put Chile in the same position as modern regulations on the subject, in the two senses described above. Regarding extension of the duty, for example, the ICCA-Queen Mary Task Force Principles on Third-Party Funding recommends that a party should "disclose the existence of a third-party funding arrangement and the identity of the funder to the arbitrators and the arbitral institution or appointing authority"[81].

With regards to the timing of the disclosure, most modern regulations require the disclosure done in the early stages of the proceeding, or as soon as possible. For example, the newly published Code of Good Practices of the Spanish Arbitration Club sets a duty of disclosure to the very late, at the statement of claim and, if the financing was received later, within a "reasonable term"[82]. Also, the Proposals for Amendment of the ICSID Rules launched by the ICSID Secretariat include a continuing obligation to disclose the name of any external funder, starting at the early stages of the process[83].

Lastly, there is controversy about how far this duty of disclosure should go. Particularly, if the terms of the TPF agreement should be disclosed. Some have argued that the terms of the TPF agreement are private and there is no regulatory need to disclose them[84]. Others have contended that full disclosure could help to determine if there are issues of usury or unconscionability in the agreement and avoid the unenforceability of the decision[85]. This article does not address this discussion because it refers to the substantial validity of the TPF agreement and other contractual relationships between funder and funded party, a subject outside its scope.

4.2.2. Second regulation: Prohibition of influencing the conduct of a claim

The second issue that has created problems refers to the control of the claim. As this essay referred to in Part 2, TPF creates incentives for the funder to influence the trial strategy in a direction that may not benefit the claimant. The influence of the funder can also create ethically conflictive incentives for legal counsel. Now we will analyse how this damaging influence can be prevented in Chile.

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81 ICCA-Queen Mary Task Force Principles on Third-Party Funding, Principle A.1.

82 Code of Good Practices of the Spanish Arbitration Club, Section VI, Duties in Relation to Financing.

83 Proposals for Amendment of The ICSID Rules, 106.

84 Queen Mary, University of London and White & Case, 2015 International Arbitration Survey: Improvements and Innovations in International Arbitration (2015), 48.

85 Ibid; Frank J. Garcia, Hyun Ju Cho, Tara Santosuosso, Randall Scarlett, and Rachel Denae Thrasher, "The Case Against Third-Party Funding in ISDS: Executive Summary", *Boston College Law School Faculty Papers* (2018), 8.

Proposed regulation to prevent undue control of the funder over the claim. To control the damaging effects of this influence, Chile needs to follow the strategy adopted by most countries that have regulated this issue. These countries have adopted either one or both of the following two rules: a prohibition for funders from influencing in any way the case strategy, and a ban for lawyers from receiving that influence.

A precise regulation adopting either of these rules would prevent the problems addressed in Part 2, the direction of the judicial system towards misplaced interests, and the ethical conflicts for lawyers. Most countries have regulated this issue through codes of conduct, either for lawyers or for funders. This way of regulating is probably the most efficient way of dealing with this issue. Self-regulation is aimed directly at the ones that exercise or receive this undue influence —the funders or lawyers—, and it is considerably less costly than the other ways of regulating.

In England and Wales is the Code of Conduct of the Associations of Litigation Funders the one that states that a funder will not "seek to influence the Funded Party's solicitor or barrister to cede control or conduct of the dispute to the Funder"[86]. In the same sense, the recently issued Honk Kong Code of Practice for Third-Party Funding of Arbitration contains a provision forbidding this influence[87]. However, as Part 3.1 of this essay explained, due to constitutional and legal limitations on freedom of association, it is ineffective to regulate through codes of conduct in Chile. This problem needs to be approached from a different standpoint.

The adequate way of addressing this issue is by passing legislation. In Chile, there is one statute that could be reformed to include a provision to prohibit this undue influence. The COT, same body that controls the independence and impartiality of adjudicators. This statute regulates most of the functioning of the judicial system in Chile and, in its Title XV, contains the regulation for lawyers. This title, among other things, establishes the academic and ethical requirements to become and practice as a lawyer in Chile and sets the basis for the legal services agreements. The Title XV of the COT can be reformed to introduce a provision that forbids lawyers from taking orders from any person that is not their client.

A provision like this would only bind lawyers because funders are not subject to the provisions directed at attorneys. However, considering that lawyers are the only ones allowed and qualified to defend someone's interest in court, the regulation would fulfil its

86 Code of Conduct of the Association of Litigation Funders of England and Wales, Section 9.3.

87 Code of Practice for Third-Party Funding of Arbitration Section 2.7.

purpose of preventing undue influence. If the lawyers are the only ones allowed to appear in court defending someone's interest, an express prohibition from taking instructions from anyone who is not their client would prevent them from accepting undue influences. ■

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