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'Security for Costs' Under the ICSID Regime: Does it Prevent 'Arbitral Hit-and-Runs' or Does it Unduly Stifle Third-Party Funded Investors' Due Process Rights?

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Abstract: This Article considers security for costs under the ICSID regime. Given that all security for costs have been ordered against third-party funded investors—with the latest decision, *Unionmatex,* in January 2020, this Article examines prior ICSID decisions to determine whether third-party funded investors are prejudiced when it comes to security for costs. It further addresses whether an applicant's right to a costs award is a "protectable right" under Article 47 and concludes that it is not. Finding that "arbitral hit-and-run" is a hypothetical concern not based on empirical evidence and providing that ICSID's new proposed rules to its Arbitration Rules will only further impede third-party funded parties' right of access to justice, this Article concludes that there is a clear prejudice against third-party funded parties. Finally, this Article concludes by reflecting that this prejudice may undermine one of the purposes for which ICSID Convention was created: to provide a forum for aggrieved investors to resolve their investment disputes—no matter how poor and regardless of whether they are funded by a third-party.

INTRODUCTION

Third-party funding (TPF)[1] has increased substantially over the past several years as a means to reduce the financial burden of bringing an investment claim.[2] For example, the global market for TPF in both litigation and arbitration is estimated as exceeding ten billion dollars.[3] Following TPF's growth, there have been concerns as to whether a party funded by a TPF will "hit" a state with arbitration and "run" without paying for a costs award since third-party funders, as non-parties to arbitration, cannot be compelled to pay costs—a scenario commonly referred to as arbitral hit-and-run.[4]

In international investment arbitration, some respondent states have resorted to security for costs to prevent this

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[1] For the purposes of this Article, "third-party funder" generally refers to any non-party, which provides funding or resources for the purpose of financing arbitration either as a donation or in return for remuneration dependent on the outcome of the proceeding; *See* Sarah Moseley, *Disclosing Third-Party Funding in International Investment Arbitration*, 97 TEX. L. REV. 1181, 1186–88 (2019).

[2] Moseley, *supra* note 1, at 1181–86.

[3] INT'L COUNCIL FOR COM. ARB., THE ICCA REPORTS NO. 4, REPORT OF THE ICCA-QUEEN MARY TASK FORCE ON THIRD-PARTY FUNDING IN INTERNATIONAL ARBITRATION 17 (2018) [hereinafter ICCA Task Report].

[4] Jennifer Trusz, *Full Disclosure? Conflict of Interest Arising from Third-Party Funding in International Commercial Arbitration*, 101 GEO. L.J. 1649, 1679 (2013) ("One concern is with the so-called "hit-and-run" scheme, whereby the claimant abuses the system via the funding relationship: the claimant will gain by succeeding in arbitration, but if it is unsuccessful, it lacks the financial ability to pay for costs").

feared outcome.[5] Security for costs, an order directing a party to set aside funds to satisfy potential adverse costs, has been a rare specimen of remedies. Up until 2014, there were no reported decisions awarding security for costs.[6] As of February 2020, there are now three known decisions all with one common denominator—the existence of TPF.[7]

Such special emphasis on TPF is also apparent in the new proposed rules to the International Centre for Settlement of Investment Disputes (ICSID)'s Arbitration Rules.[8] While only three known decisions have awarded security for costs, ICSID has made it a priority to include a stand-alone provision just for security for costs.[9] If adopted, parties will be required to affirmatively disclose their third-party funder,[10] and tribunals will be endowed with authority to dismiss proceedings if a party fails to comply with a security for costs order.[11] Combined with their express innuendo

[5] *See* Laurence Craig, *Some Trends and Developments in the Laws and Practice of International Commercial Arbitration*, 50 TEX. INT'L L.J. 699, 754–55 (2016) ("The possibility that an unsuccessful party may, in a final decision on the merits of the case, be required to contribute to the costs of his adversary is recognized in a number of legal systems, and indeed the ICC Rules permit arbitrators to make such an award").

[6] Chiara Cilento & Benjamin Guthrie, *Is Investor-State Arbitration Warming up to Security of Costs?*, KLUWER ARBITRATION BLOG (June 18, 2019), http://arbitrationblog.kluwerarbitration.com/2019/06/18/is-investor-state-arbitration-warming-up-to-security-for-costs/ ("The order of security for costs affirmed by the RSM ad hoc committee was hailed as groundbreaking when it was published in 2014. No investment tribunal had previously issued such an order.").

[7] *See generally* Cilento & Guthrie, *supra* note 6.

[8] INT'L CTR. FOR SETTLEMENT OF INV. DISPS., WORKING PAPER #4, PROPOSALS FOR AMENDMENT OF THE ICSID RULES 58–59 (2020) [hereinafter ICSID WORKING PAPER 4], https://icsid.worldbank.org/sites/default/files/WP_4_Vol_1_En.pdf. Note: the proposed rules for ICSID's Arbitration Rules begin on page 27.

[9] ICSID WORKING PAPER 4, *supra* note 8, at 58-59. (Proposed Rule 53).

[10] ICSID WORKING PAPER 4, *supra* note 8, at 37-38. (Proposed Rule 14).

[11] ICSID WORKING PAPER 4, *supra* note 8, at 58-59. (Proposed Rule 53(6)).

that TPF is a factor to justify ordering security for costs,[12] the proposed rules raise significant due process consequences for third-party funded parties as well.

Given that arbitral hit-and-run concerns are not empirically supported by previous incidents but rather rest on a "what-if" scenario, and since there are other measures to filter out unmeritorious claims, this Article posits that security for costs addresses a *hypothetical* concern at the cost of investors' *real* due process rights.

Part I of this Article sets the stage by introducing security for costs and providing two opposing interests underlying security for costs: "arbitral hit-and-run" concerns and a party's right of access to justice. Part II introduces Article 47 of the ICSID Convention and Rule 39 of the ICSID Arbitration Rules and their applicability to security for costs. Part III demonstrates that previous decisions have failed to address whether adverse costs are "rights" entitled to preservation under Article 47 and proposes that adverse costs are not protectable rights. Part IV provides that "arbitral hit-and-run" concerns are not based on any empirical evidence and thus unwarranted. Part V delineates pertinent Proposed Rules to the ICSID's Arbitration Rules and concludes that, if adopted, they would further impede third-party funded parties' access to due process.

I. SECURITY FOR COSTS

A. SECURITY FOR COSTS

"Security for costs" is a form of provisional measure, which orders a party to post security to cover the applicant's expected costs in defending itself against the claim.[13] The

[12] ICSID WORKING PAPER 4, *supra* note 8, at 58-59. (Proposed Rule 53(4)).
[13] SARAH BREWIN, BEST PRACTICES SERIES: SECURITIES FOR COSTS 1 (INT'L

aim is to protect parties from the unfortunate outcome in which they bear legal costs to defend unmeritorious claims but cannot collect a potential costs award due to the other party's inability or unwillingness to pay.[14]

B. ARBITRAL HIT-AND-RUN V. RIGHT OF ACCESS TO JUSTICE

Arbitral hit-and-run has been defined as a situation "where the claimant's arbitration fees and expenses are being covered by a related entity or individual who stands to gain if the claimant wins, but who would not be liable to meet any award of costs that might be made against the claimant if it lost."[15] On the other hand, there is a legitimate concern that security for costs may burden a party's right of access to justice.[16] For a claimant who is going through financial difficulties, perhaps due to a state's misappropriation, posting security may be impossible where costs of international investment arbitration can reach tens of millions of U.S. dollars.[17] Failing to comply with a securities order may result in a termination of proceedings—exemplifying the serious impact that security for costs may have on a claimant's due process rights.[18]

INST. FOR SUSTAINABLE DEV. (IISD) Oct. 2018).

[14] BREWIN, *supra* note 13.

[15] J.E. Kalicki, *Security for Costs in International Arbitration*, TRANSNAT'L. DISPUTE MGMT. 3 (2006), https://www.transnational-dispute-management.com/article.asp?key=827.

[16] *See* Jean-Baptiste Pessey, *When to Grant Security for Costs in International Commercial Arbitration: the Complex Quest for a Uniform Test*, CPR INT'L INST. FOR CONFLICT PREVENTION & RESOL. (May 6, 2011), https://www.cpradr.org/news-publications/articles/2011-05-06-when-to-grant-security-for-costs-in-international-commercial-arbitration-the-complex-quest-for-a-uniform-test-2011-writing-contest-winner.

[17] DAVID GOLDBERG ET AL., 2019 EMPIRICAL STUDY: PROVISIONAL MEASURES IN INVESTOR-STATE ARBITRATION, BRITISH INST. OF INT'L & COMPAR. L. 14 (White & Case, 2019).

[18] RSM Production Corporation v. Saint Lucia, ICSID Case No. ARB/12/10, Decision on Annulment, ¶¶ 145-148 (Apr. 29, 2019).

II. THE ICSID CONVENTION ON "SECURITY FOR COSTS"

A. ARTICLE 47 AND RULE 39 OF THE ICSID CONVENTION

Under the current ICSID regime, there is no rule particular to security for costs.[19] Rather, they operate under ICSID Convention's Section 3, Article 47 (Article 47) and ICSID's Arbitration Rule 39, which govern all forms of provisional measures.[20] Article 47 of the ICSID Convention allows a tribunal to order any provisional measure to preserve a party's rights.[21] Under Rule 39 of the ICSID Arbitration Rules, any party may request a tribunal for a provisional measure by "specify[ing] the rights to be preserved, the measures the recommendation of which is requested, and the circumstances that require such measures."[22]

Because these rules are construed broadly, prior ICSID cases have served as persuasive law for tribunals when determining whether to order security for costs.[23] While there is no doctrine of precedent—or *stare decisis*—in ICSID arbitration, previous decisions have served a similar function to compensate for the lack of guidance.[24] When addressing security for costs, tribunals have generally applied the same requirements as for other provisional

[19] Sam Luttrell, *Observations on the Proposed new ICSID Regime for Security for Costs*, 36 J. INT'L ARB. 3, 3–5 (2019).
[20] INT'L CTR. FOR SETTLEMENT OF INV. DISP., ICSID CONVENTION, REGULATION AND RULES 24, 118, https://icsid.worldbank.org/sites/default/files/ICSID%20Convention%20English.pdf. [hereinafter ICSID RULES].
[21] ICSID RULES, *supra* note 20, at 24 (ICSID Convention, Article 47).
[22] ICSID RULES, *supra* note 20, at 118 (ICSID Arbitration Rules, Rule 39).
[23] Luttrell, *supra* note 19.
[24] Luttrell, *supra* note 19.

measures: (i) identification of the rights to be preserved, (ii) requested measures to protect that interest, and (iii) circumstances[25] that require such measures.[26] But for security for costs, there has been one clear distinction, which is requiring an "exceptional circumstance."[27]

B. "EXCEPTIONAL CIRCUMSTANCES": MATERIAL RISK THAT COST AWARD WILL NOT BE COMPLIED WITH

While each tribunal attaches a different test to determine whether an exceptional circumstance exists, there is a general consensus for securities for costs—there must be a material risk that adverse costs will not be complied with.[28] In all three decisions ordering security for costs, the existence of a TPF arrangement played a crucial factor, albeit not the sole factor.

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[25] Occidental Petroleum Corporation v. Republic of Ecuador, ICSID Case No. ARB/06/11, Decision on Provisional Measures, ¶ 59 (Aug. 17, 2007) ("circumstances" defined as those for which "the measures are *necessary* to preserve a party's rights and where the need is *urgent* in order *to avoid irreparable harm*").

[26] ICSID RULES, *supra* note 20, at 118 (ICSID Arbitration Rules, Article 39(1)):

> At any time after the institution of the proceeding, a party may request that provisional measures for the preservation of its rights be recommended by the Tribunal. The request shall specify the rights to be preserved, the measures the recommendation of which is requested, and the circumstances that require such measures.

[27] Luttrell, *supra* note 19, at 4-5.

[28] RSM Prod. Corp. v. Saint Lucia, ICSID Case No. ARB/12/10, Decision on St. Lucia's Request for Security for Costs, ¶¶ 77–82 (Aug. 12, 2014); Dirk Herzig as Insolvency Administrator over the Assets of Unionmatex Industrieanlagen GmbH v. Turkmenistan (hereinafter "Unionmatex"), ICSID Case No. ARB/18/35, Decision on the Respondent's Request for Security for Costs and the Claimant's Request for Security for Claim, ¶¶ 53–58 (Jan. 27, 2020).

RSM Production Co. v. St. Lucia was the first known occasion in which security for costs was ordered.[29] In 2014, the *RSM* majority tribunal granted St. Lucia's request, finding that (i) the claimant's history of non-compliance with costs awards in prior ICSID cases, (ii) its poor financial status, and (iii) the existence of TPF created a material and urgent risk that the claimant would not reimburse St. Lucia—creating an "exceptional circumstance."[30] While *RSM* serves as a "landmark" case as the first decision to order security for costs against a third-party funded party, the existence of TPF seemed to have served as only an ancillary factor, and the tribunal weighed the claimant's prior history of non-compliance heavily in ordering security for costs.[31] The *RSM* proceeding was dismissed with prejudice when claimant failed to comply with the security for cost order.[32]

Four years later, in 2018, the second known security for costs order was issued in *Armas v. República Boliviariana de Venezuela*.[33] Relying on the *RSM* decision, the *Armas* tribunal found that an exceptional circumstance existed since (i) the claimants were funded by TPF, (ii) the claimants did not have the resources to pay the adverse costs order, and (iii) the underlying TPF arrangement precluded the funder from any cost liability.[34]

Finally, *Unionmatex v. Turkmenistan* is the third and last known decision to order security for costs, which was

[29] RSM Prod. Corp., *supra* note 28, at ¶¶ 27, 53–54.
[30] RSM Prod. Corp., *supra* note 28, at ¶¶ 77-84.
[31] RSM Prod. Corp., *supra* note 28, at ¶¶ 81-82.
[32] RSM Prod. Corp., *supra* note 18 (The Decision on Annulment).
[33] Armas v. República Boliviariana de Venezuela, PCA Case No. 2016-08, Decision on Request for Security for Costs, ¶ 261 (June 20, 2018).
[34] Armas, *supra* note 33, at ¶¶ 199, 243–44, 250.

rendered in January 2020.[35] In this case, which is still ongoing, a third-party funded claimant brought a claim against Turkmenistan alleging that its misappropriation caused its insolvency.[36] The majority tribunal granted Turkmenistan's application for security for costs and found that an exceptional circumstance existed on the following grounds: (i) the claimant was insolvent, (ii) the existence of TPF, and (iii) the funding arrangement explicitly absolving the funder from cost liability, the same factor existing in *Armas*.[37] Here, the third factor—TPF arrangement absolving the funder from adverse cost liability—was found to create a "more extreme situation."[38] Reasoning that neither the claimants nor the third-party funder would be able to pay adverse costs due to the party's impecuniosity or the funder's non-liability for costs, the tribunal found that an exceptional circumstance existed.[39]

C. PREJUDICE AGAINST THIRD-PARTY FUNDED PARTIES

Until the *RSM* decision in 2014, not only were there no decisions ordering security for costs in international investment arbitration, but there were also no TPFs involved in those cases.[40] Prior to *RSM*, the consistent view of tribunals addressing security for cost has been that there is no financial requirement to proceed in ICSID arbitration,[41]

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[35] Unionmatex, *supra* note 28.
[36] Unionmatex, *supra* note 28, at ¶ 1.
[37] Unionmatex, *supra* note 28, at ¶¶ 57-58.
[38] Unionmatex, *supra* note 28, at ¶ 57.
[39] Unionmatex, *supra* note 28, at ¶¶ 57–60.
[40] For the purpose of this Article, sixteen reported ICSID security for cost decisions were examined.
[41] Grynberg et al. v. Grenada, ICSID Case No. ARB/10/6, Tribunal's Decision on Respondent's Application for Security for Costs, ¶ 5.19 (October. 14, 2010) ("[I]t is simply not part of the ICSID dispute resolution system that an investor's claim should be heard only upon the establishment of a sufficient standing of the investor to meet a possible costs award"); Burimi et al. v. Republic of

emphasizing the serious risk that such an order would have in stifling a claimant's right to due process.[42]

It was not until *RSM*, *Armas*, and *Unionmatex* that TPF arose as a factor which helped to justify a securities for costs order.[43] In *RSM*, the tribunal reasoned that the existence of TPF supports its concern that the claimant would not comply with a costs award since "it is doubtful whether the third party will assume responsibility for honoring such an award."[44] In *Armas* and *Unionmatex,* the TPF arrangement precluding the funder from costs liability served as a determinative factor on the ground that, without the funder, no one would be able to pay adverse costs.[45]

However, this scenario is not different from a scenario in which there is only an insolvent party and no TPF. In both scenarios, the risk of the applicant's non-collection of costs is the same—"either way, [the applicant] would not receive an ordered reimbursement of its costs."[46] Since tribunals

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Albania, ICSID Case No. ARB/11/18, Procedural Order No.2, ¶ 41 (May 3, 2012) ("Tribunal would be reluctant to impose on the Claimants what amounts to an additional financial requirement as a condition for the case to proceed"); EuroGas Inc. v. Slovak Republic, ICSID Case No. ARB/14/14, Procedural Order No.3, ¶ 123 (June 23, 2015); Lighthouse Corp. v. Democratic Republic of Timor-Leste, ICSID Case No. ARB/15/2, Procedural Order No.2, ¶ 60 (Feb. 13, 2016) ("[T]here is no requirement in the ICSID system that a claimant must demonstrate its solvency").

[42] Gustav F W Hamester GmbH & Co KG v. Republic of Ghana, ICSID Case No. ARB/07/24, Award ¶ 17 (June 18, 2010) (Application or a security for cost order rejected on the ground that "there was a serious risk that an order for security for costs would stifle the claimant's claims . . . .").

[43] RSM Prod. Corp., *supra* note 28, at ¶ 83; Armas, *supra* note 33. Unionmatex, *supra* note 28, at ¶¶ 53–62.

[44] RSM Prod. Corp., *supra* note 28, at ¶ 83.

[45] Unionmatex, *supra* note 28, at ¶¶ 53–62.

[46] Lars Markert, *Security for Costs Applications in Investment Arbitrations Involving Insolvent Investors*, 11(2) CONTEMP. ASIA ARB. J. 217, 231 (Dec. 13, 2018), available at: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3295803 (last accessed March 30, 2020).

have held a party's impecuniosity to be insufficient to order security for costs,[47] the existence of TPF or its terms should not make a difference. The fact that the term absolving the third-party funder from cost liability was in the limelight of *Armas* and *Unionmatex* shows inherent prejudice against third-party funded parties since the feared scenario of no one being liable to pay costs at the end of arbitration would be the same if there was just an insolvent investor and no TPF. If there is no requirement for a claimant to prove its financial standing to proceed with ICSID arbitration, then the same protection should be afforded to those who are funded by TPF—regardless of whether their funder is liable for costs.

III. PUTTING THE HORSE BEFORE THE CARRIAGE

Further, tribunals granting security for costs have missed the more fundamental gateway issue of whether a "right" entitled to preservation exists in the first place. *Eskosol, Anderson, and Lighthouse* tribunals acutely noted that "the starting point is identification of the particular 'rights' that the applicant claims are appropriate to be preserved"—which is to precede any decisions on whether "exceptional circumstances" exist.[48] However, decisions ordering security for costs have blindly accepted that security for costs qualifies as a right to be preserved.[49]

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[47] Grynberg, *supra* note 41, at ¶ 5.19.

[48] Eskosol S.P.A. in Liquidazione v. Italian Republic, ICSID Case No. ARB/15/50, Procedural Order No.3, ¶ 32 (Apr. 12, 2017); *see also* Anderson v. Republic of Costa Rica, ICSID Case No. ARB(AF)/07/3, Decision on Provisional Measures, ¶ 23 (Nov. 5, 2008) ("[A]t this point in the proceeding, the Respondent has not proven the existence of any rights whose preservation requires the requested provisional measures."); Lighthouse Corp., *supra* note 41, at ¶ 56 ("The first requirement for provisional measures is that the latter seek to preserve rights of the applicant").

[49] RSM Prod. Corp., *supra* note 28, at ¶¶ 72-74; Unionmatex, *supra* note 28, at ¶¶ 51–52.

For example, in *RSM*, the majority tribunal limited its findings of a protectable "right" to the bare-bone holding that "conditional rights such as the potential claim for cost reimbursement qualify as 'rights to be preserved.'" [50] Similarly, the *Unionmatex* tribunal made a simple conclusory statement that "*Turkmenistan* has specified the right to be preserved."[51] Since provisional measures would not be available without "rights" to be "preserved", these decisions indeed "put the horse before the carriage."[52]

A. ADVERSE COSTS – NOT A PROTECTABLE RIGHT

Security for costs reflects the applicant's alleged "right" to adverse costs. In 2017, the *Eskosol* tribunal first raised the question of whether a party's asserted "right" to collect a possible costs award is one that is protectable.[53] Notable authorities have also noted this gateway issue raised by *Eskosol* as one that is emerging and complex. However, ICSID tribunals or other authorities are yet to address this issue.[54] Even in *Eskosol*, the tribunal did not answer this question, holding that the *Eskosol* applicant would not be entitled to security for costs even if it had a protectable right. [55] This Article addresses *Eskosol*'s unanswered question by dividing provisional measures into two categories: those protecting procedural rights and those protecting substantive rights.[56] This distinction is crucial since a provisional measure (*e.g.*, security for costs) must

[50] RSM Prod. Corp., *supra* note 28, at ¶¶ 72-74.
[51] Unionmatex, *supra* note 28, at ¶ 52.
[52] ICSID RULES, *supra* note 20, at 24 (ICSID Convention, Article 47); ICSID RULES, *supra* note 20, at 118 (ICSID Arbitration Rules, Rule 39).
[53] Eskosol, *supra* note 48, at ¶¶ 32-36.
[54] Markert, *supra* note 46, at 225.
[55] Eskosol, *supra* note 48, at ¶ 36.
[56] RSM Prod. Corp., *supra* note 28, at ¶ 69 ("The predominant objective of provisional measures is to protect the integrity of the proceedings. This integrity comprises both substantive and procedural rights"); Lighthouse Corp., *supra* note 41, at ¶ 56 ("These rights can be substantive or procedural in nature").

serve the function of protecting either of the two rights. This Article concludes that a party's right to adverse costs are not protectable since it is neither a procedural right nor a substantive right.

(i) PROCEDURAL RIGHTS

Procedural rights are those that are related to a party's path to pursue its claim or defense.[57] Compelling witness attendance and preservation of evidence fall under this category—for example, certain evidence may be required to satisfy an essential element of a party's claim. By definition, procedural rights: (i) exist at the time of the application and (ii) preservation of these rights must serve a procedural function for the party's pursuit of the claim.

In *RSM*, security for costs was categorized as a "procedural right."[58] However, security for costs does not fit into this category. First, there are no existing rights to adverse costs since costs are awarded at the end of arbitration. Second, security for costs does not serve a procedural function. As the *Eskosol* tribunal noted, presence or absence of assets to satisfy a possible adverse costs order does not impede a party's path to obtain a favorable award.[59] As such, the *Eskosol* tribunal determined that security for cost is "not truly a concern about a procedural right but instead an outcome-related worry about collection on such effective relief."[60]

[57] Eskosol, *supra* note 48, at ¶ 33.
[58] RSM, *supra* note 28, at ¶ 64 ("the right invoked by Respondent can be qualified as a *procedural* right not directly related to the subject matter of the dispute.").
[59] Eskosol, *supra* note 48, at ¶¶ 32-33.
[60] Eskosol, *supra* note 48, at ¶ 33.

(ii) SUBSTANTIVE RIGHTS

Since adverse costs do not protect a "procedural right", adverse costs must fall under the "substantive right" category in order to give rise to a provisional measure. Substantive rights are those that are related to the subject matter of the dispute.[61] Often referred to as a measure to protect a party's "right to an effective relief," "maintaining the status quo," or "preventing further aggravation," substantive rights are those that ensure that a party's rights relating to the subject matter of the dispute will be preserved until the final resolution.[62] The intent is to ensure that any final award on the merits is not impaired by acts taken by the other party during the pendency of deliberation. Unlike procedural rights, substantive rights need not exist at the time of application and may be conditional on prevailing in arbitration—as long as the right relates to the dispute.[63] For the purposes of this Article, non-existing substantive rights shall be referred to as "conditional rights," which is to be distinguished from "hypothetical rights."[64]

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[61] Amco v. Republic of Indonesia, ICSID Case No. ARB/81/1, Decision on Request for Provisional Measures, ¶ 3 (Dec. 9, 1983) (provisional measures only protect "rights in dispute"); Plama v. Bulgaria, ICSID Case No. ARB/03/24, Order, ¶ 39 (Sept. 6, 2005) (provisional measures protect "rights relating the dispute").

[62] Amco, *supra* note 61, at ¶ 3; Plama, *supra* note 61, at ¶ 39.

[63] Occidental Petroleum Corp., *supra* note 25, at ¶ 63 (Aug. 17, 2007) (claimants "need only show that they allege the kind of claims that—if proven—would entitle claimants to substantial relief").

[64] Occidental Petroleum Corp., *supra* note 25, at ¶ 89 (holding that provisional measures are "not meant to protect against any potential or hypothetical harm susceptible to result from uncertain actions"); *See also* Anderson, *supra* note 48, at ¶ 23 (denying an application for a security for costs order on the ground that "[r]espondent has only a mere expectation" and "has not proven the existence of any rights whose preservation requires the requested provisional measures").

a. "Conditional" Substantive Rights

A "conditional right" can be construed to denote a right, the existence of which is certain to arise when the applicant prevails. *Lao Holdings v. The Government of the Lao People's Democratic Republic* is instructive in defining what constitutes a "conditional right."[65] In *Lao Holdings*, the dispute was whether the claimant was entitled to extend its agreement with the Lao government, which would have sheltered the claimant from the Lao government's high tax rates.[66] The claimant sought a provisional measure seeking to enjoin the Lao government from any attempts to collect its taxes and from seizing the claimant's property until the resolution of the dispute.[67] In granting claimant's request, the *Lao Holdings* tribunal noted that the "right to be preserved" need not exist at the provisional measures stage.[68] Here, the claimant's non-liability for Lao's taxes was a "conditional right" since it would have certainly arisen if the claimant prevailed (*i.e.*, the claimant was entitled to extend its agreement with the government).

b. "Hypothetical" Substantive Rights

On the other hand, a "hypothetical right" refers to those rights, the occurrence of which depends on factors additional to prevailing in arbitration.[69] This term was first coined in a 1999 ICSID decision, *Maffezini v. Kingdom of Spain*.[70] Here, the tribunal recognized that security for costs would

[65] Lao Holdings v. The Government of the Lao People's Democratic Republic, ICSID Case No. ARB (AF)/12/6, Decision on Claimant's Amended Application for Provisional Measures (Sept. 17, 2013).
[66] Lao Holdings, *supra* note 65, at ¶¶ 7-8.
[67] Lao Holdings, *supra* note 65, at ¶ 9.
[68] Lao Holdings, *supra* note 65, at ¶ 16.
[69] *See* Maffezini v. The Kingdom of Spain, ICSID Case No. ARB/97/7, Procedural Order No. 2, ¶¶ 16-18 (Oct. 28, 1999).
[70] Maffezini, *supra* note 69, at ¶¶ 13-18.

be based on a "hypothetical right" not entitled to a provisional measure. Specifically, the tribunal recognized that security for costs would be based on a "hypothetical right" by noting that ordering security for costs would require making two merit-based assumptions: (1) the applicant will prevail ***and*** (2) the applicant will "deem the claimant's case to be of such nature as to require it to pay [adverse costs,]" which would be inappropriate at that stage.[71] The *Maffezini* tribunal's recognition is important because it captures the delicate conundrum with security for costs orders - - they seek to protect a right that will ***not*** come into existence solely by the applicant's prevailing on the merits but, rather, they will only come into existence if the applicant prevails ***and*** if the applicant also convinces the tribunal that it is entitled to costs of the arbitration (*i.e.*, a "hypothetical right"").

Despite the crucial distinction between "conditional rights" and "hypothetical rights", ICSID tribunals ordering security for costs failed to recognize this delicate distinction. This failure is important because the *RSM* decision, the first to order security for costs, is premised upon the overly simple proposition that "rights to be preserved by a provisional measure need not already exist at the time the request is made" and that "conditional rights such as the potential claim for cost reimbursement" are protectable.[72] While the *RSM* tribunal recognized the difference between existing and conditional rights, it failed to recognize that some rights are conditional and hypothetical. Following *RSM*, two other ICSID tribunals relied on *RSM* for this proposition in addressing security for costs applications.[73] This is

[71] Maffezini*, supra* note 69, at ¶¶ 16-17.
[72] RSM Prod. Corp., *supra* note 28, at ¶ 72.
[73] BSG Resources Ltd. v. Republic of Guinea*,* ICSID Case No. ARB/14/22*,* Procedural Order No. 3, ¶ 75 (Nov. 25, 2015) ("[W]hile the Tribunal acknowledges that the right requiring preservation relies on two hypothetical events (that the Respondent will prevail in this arbitration and that it will be

troubling since the *RSM* tribunal fails to distinguish between "conditional rights" and "hypothetical rights" and by this definition, any right would be protectable—even those based on conjectures and speculations.

A party's entitlement to adverse costs is not a substantive right because it is not related to the subject matter of the dispute. By way of example, in the *Lao Holdings* case, the respondent (*i.e.*, Lao government)'s attorney fees would not relate to whether the claimant was entitled to extend their agreement. Further, a party's right to adverse costs is not a "conditional right" since prevailing in arbitration would not give rise to adverse costs.[74] As summarized by one of the *Unionmatex* arbitrators, adverse costs are only awarded if a party prevails *and* persuades the tribunal that the unsuccessful party (a) advanced patently unmeritorious or legally untenable claims, (b) abused the investment arbitration process, (c) presented poor and inefficient pleadings, or (d) engaged in egregious underlying conduct.[75] In fact, successful parties were reported to recover costs in only sixty-one percent of ICSID cases.[76]

Since a party's right to adverse costs is neither a procedural right nor a substantive right, it cannot be a right that is protectable within the meaning of Article 47 -- a crucial gateway issue that tribunals granting security for costs have

awarded costs), it nevertheless deems that the *prima facie* existence of a right has been established."); Lighthouse Corp., *supra* note 41, at ¶ 57.

[74] Anderson, *supra* note 48, at ¶ 26 ("At this point in proceeding, the Respondent cannot be considered to be a holder of a legal right, but only the bearer of a mere expectation [to adverse costs]").

[75] Lucy Reed, *Allocation of costs in international arbitration*, 26 ICSID REV.: FOREIGN INVESTMENT L.J. 76, 84 (2011).

[76] Matthew Hodgson, *Investment Treaty Arbitration: Cost, Duration and Size of Claims All Show Steady Increase*, ALLEN & OVERY (Dec. 14, 2017), https://www.allenovery.com/en-gb/global/news-and-insights/publications/investment-treaty-arbitration-cost-duration-and-size-of-claims-all-show-steady-increase.

failed to distinguish. This Article proposes that the distinction between "conditional rights" and "hypothetical rights" is significant because while both rights refer to future, contingent events, only the former is protectable. This failure to distinguish between protectable and non-protectable rights has directly prejudiced third-party funded parties since they have been the only victims to security for costs thus far.

This Article does not propose, however, that all securities for costs existing in international arbitration are invalid. Instead, it merely posits that securities for cost orders in the ICSID system present a problem because adverse costs are not protected rights within the meaning of Article 47.

B. "MERITS" – NOT CONSIDERED OR PRESUMED IN FAVOR OF THE STATE?

Not only do securities for costs protect a right that should not be protectable under Article 47, there is also a subtle, yet powerful presumption that warrants attention. Tribunals granting security for costs essentially make merit-based assumptions in favor of applicants, including assumptions that: (i) applicants will prevail; and (ii) applicants will be awarded cost awards. However, they do not afford claimants the same privilege. The *Unionmatex* tribunal, for example, refused to consider a claimant's assertion that Turkmenistan's acts caused its insolvency, claiming it as a "merits" issue subject to later assessment.[77] This imbalance is significant because investors may face an early termination of their proceedings before they have a chance to prove states' wrongful acts.

[77] Unionmatex, *supra* note 28, at ¶ 66.

In regard to this, the *Unionmatex* claimant made a comical, but strong point that security for costs ordered against it would encourage host states to "do the job right" to "better ensure the investor's insolvency and prevent any BIT claim from the outset."[78] While this may sound comical at first, it is not entirely inconceivable, especially for investors whose assets are stripped away by states' wrongful acts. It may turn the David and Goliath biblical story into a reality, except Goliath's acts would be allowed to proceed without legal repercussions.[79]

IV. 'ARBITRAL HIT-AND-RUN' *- JUMPING THE GUN*

As noted above, the concern underlying "arbitral hit-and-run" is that applicants will have to expend significant costs to defend an unmeritorious claim but will be left with no means to collect potential cost awards.[80] The idea is that investors, with the help of TPF, will indiscriminately "hit" states with arbitral proceedings with the hope that one sticks, and if it doesn't prevail, it will "run," leaving no one to satisfy the cost award.[81] However, this concern is unwarranted on three points: (1) third-party funders do not fund unmeritorious claims—in fact, the existence of TPF shows good prospects of success given the high level of due

[78] Unionmatex, *supra* note 28, at ¶ 37.
[79] Unionmatex, *supra* note 28, at ¶ 66:

> The Tribunal must ignore Dr Herzig's allegation that it is unreasonable for Turkmenistan to obtain security for costs when it was Turkmenistan that allegedly caused the insolvency of Unionmatex. This is plainly a merits issue, subject to later assessment and one on which the Tribunal expresses no view at this stage.

[80] Trusz, *supra* note 4.
[81] Kalicki, *supra* note 15.

diligence a claim undergoes in order to be funded;[82] (2) ICSID rules have many other effective mechanisms to filter out unmeritorious claims—which don't involve penalizing claimants for their financial status—including "screening for manifest lack of jurisdiction before registration of a request, a motion to dismiss for manifest lack of legal merit and bifurcated preliminary motions";[83] and (3) there is no empirical evidence supporting "arbitral hit-and-runs." Only one case was found to allegedly support an "arbitral hit-and-run," *S&T Oil v. Romania,*[84] which was not really an "arbitral hit-and-run" case. In *S&T Oil*, the case was discontinued because the third-party-funded claimant failed to pay advance on costs after its TPF withdrew from the case.[85] Thereafter, there were notions made to the effect that this situation could have quickly turned into a scenario where the respondent could not have been able to recover its costs,[86] and that security for costs could somehow have been the solution. This is what, in America, is referred to as "jumping the gun, *i.e.*, making a decision that is premature." In *S&T*, the case was discontinued from the claimant's failure to pay advance costs and, in any event, the claimant

[82] ICCA Task Report, *supra* note 3, at 25 (TPF Applications have suggested rejection rates of 90% or higher, and applications undergo a detailed due diligence in order to ensure that there is a "solid claim with a healthy recoverable margin"); *Third Party Funding in International Arbitration*, ASHURST (Feb. 21, 2020), https://www.ashurst.com/en/news-and-insights/legal-updates/quickguide---third-party-funding-in-international-arbitration/.

[83] *Proposals for Amendment of the ICSID Rules—Working Paper*, 131 at ¶ 242 (Aug. 2, 2018).

[84] S&T Oil Equipment and Machinery Ltd. v. Romania, ICSID Case No. ARB/07/13, Order of Discontinuance of the Proceeding (July 16, 2010).

[85] S&T Oil, *supra* note 84, at ¶ 32*; See* Umika Sharma, *Third Party Funding in Investment Arbitration: Time to Change Double Standards Employed for Awarding Security for Costs?,* KLUWER ARB. BLOG (July 29, 2018), http://arbitrationblog.kluwerarbitration.com/2018/07/29/third-party-funding-investment-arbitration-time-change-double-standards-employed-awarding-security-costs/.

[86] Sharma, *supra* note 85.

would not have been able to proceed with the case.[87] Since this is the only case found to form the basis for "arbitral hit-and-run," there is a legitimate question as to whether this is merely a premature worry based on a hypothetical situation instead of actual cases.

V. ICSID CONVENTION'S PROPOSED CHANGES

Against this backdrop, the new Proposed Rules (PR) to the ICSID Convention's Arbitration Rules,[88] if adopted, would lower the threshold to obtain security for costs while making other provisional measures more difficult. Pertinently, PR 14 would require parties to affirmatively disclose their TPF arrangement, and tribunals may order disclosure of TPF terms.[89] While disclosure of a party's third-party funder may be useful to prevent any conflict of interest issues that may arise between funders and arbitrators, tribunals' authority to disclose TPF terms seems problematic, especially given that a TPF term absolving the funder from cost liability was the determinative factor in the *Unionmatex* and *Armas* tribunals' decisions to order security for cost.[90]

Further, securities for cost would have their own stand-alone provision under PR 53 and it is not in the third-party funded parties' best interests.[91] First, under PR 53(4), TPF is out rightly put under an unfavorable light with its mandate that TPF "may not by itself be sufficient to *justify* an order for security for costs."[92] While this rule seems to have the best interests of third-party funded parties at heart, it is really a

[87] *See* S&T Oil, *supra* note 84.
[88] ICSID WORKING PAPER 4, *supra* note 8.
[89] ICSID WORKING PAPER 4, *supra* note 8, at 37-38. (Proposed Rule 14).
[90] Unionmatex, *supra* note 28, at ¶¶ 57–60.
[91] ICSID WORKING PAPER 4, *supra* note 8, at 58-59. (Proposed Rule 53).
[92] ICSID WORKING PAPER 4, *supra* note 8, at 58-59. (Proposed Rule 53(4)).

knife in disguise. The word "justify" draws a negative inference for TPF. It presupposes that TPF would certainly be a factor in favor of ordering security for costs if it were accompanied by another factor. Second, PR 53(6) would endow tribunals with the authority to dismiss proceedings if a party fails to comply with a security for cost order.[93] This is meaningful given that, under the current rules, the only express grounds for suspension of a proceeding are for vacancy, lack of jurisdiction and arbitrator disqualification,[94] none of which penalize a claimant for its financial conditions. Last but certainly not least, PR 53 does not require a "rights to be preserved," lowering the threshold for security for costs even more.[95]

Meanwhile, all other forms of provisional measures would be governed by PR 47, which provides more detailed guidance on what warrants provisional measures by listing non-exhaustive circumstances giving rise to provisional measures (*e.g.*, prevent imminent harm).[96] While provisional measures are not restricted to these circumstances, it nevertheless demonstrates the kind of extraordinary situations that prompt provisional measures.[97] Second, PR 47(3) explicitly requires tribunals to consider whether provisional measures are "urgent" and "necessary," which is not always considered by tribunals.[98] For example, the *Unionmatex* tribunal found that urgency is not a requirement in issuing security for costs.[99] They seem to

[93] ICSID WORKING PAPER 4, *supra* note 8, at 58-59. (Proposed Rule 53(6)).
[94] ICSID Convention, Regulations and Rules (2006), Rules 9(6), 10(2), 29(3); ICSID Arbitration Rule 41.
[95] ICSID WORKING PAPER 4, *supra* note 8, at 58-59. (Proposed Rule 53).
[96] ICSID WORKING PAPER 4, *supra* note 8, at 54-55. (Proposed Rule 47(1)(a)).
[97] ICSID WORKING PAPER 4, *supra* note 8, at 54-55. (Proposed Rule 47(1)).
[98] ICSID WORKING PAPER 4, *supra* note 8, at 54-55. (Proposed Rule 47(3)(a)).
[99] Unionmatex, *supra* note 28, at ¶ 67:

> Insofar as the element of urgency is concerned, the Tribunal is not persuaded that Turkmenistan must prove an urgent need for

disparately treat security for costs apart from other forms of provisional measures -- in order to make provisional measures more difficult to obtain while ensuring that securities for costs remain easier to obtain.

Third-Party disclosure—great. The ICSID Convention would be better prepared for the likely growth of TPF by preventing potential conflict-of-interest issues. But the innuendo that TPF is a factor justifying security for cost combined with the tribunal's new-found authority to dismiss proceedings upon non-compliance—maybe not so much. Together, they carry significant due process consequences for third-party funded claimants. Further, failure to reciprocate changes in Proposed Rule 47 to Proposed Rule 53 should not be ignored. If adopted, these proposed rules would serve the function of filtering out third-party funded claims early on, for impecunious claimants, without any regard to their assertion that the state's misconduct caused their impecuniosity. In light of prior decisions, one cannot help but feel that the Proposed Rules are, and dare I say it, a witch-hunt for third-party funded parties.[100]

> the provisional measure of security for costs. In any event, given that the arbitration remains at an early stage with the final evidentiary hearing not scheduled until September 2021, the Tribunal perceives no urgency.

[100] A similar attitude to a "witch-hunt" was captured by one member of the *RSM* tribunal. *See* RSM Prod. Corp., *supra* note 28, at ¶ 18 (Assenting reasons):

> My determinative proposition is that once it appears that there is third party funding of investor's claims, the onus is cast on the claimant to disclose all relevant factors and make a case why security for costs orders should not be made.

CONCLUSION

Based on the previous three ICSID cases ordering security for costs and ICSID Convention's Proposed Rules, there is a recurring theme—TPF. With growing appearances of third-party funded parties in ICSID arbitration, the tribunals' uniform position that there is no financial requirement to proceed in ICSID arbitration seemed to have shifted, as demonstrated by *RSM*, *Armas* and *Unionmatex*, revealing their critical stance towards TPF. Additionally, the above tribunals' conclusory finding that adverse costs are "protectable rights" within the meaning of Article 47 was akin to putting the horse before the carriage since provisional measures are only available for protectable rights. This Article sought to address the *Eskosol* tribunal's unanswered question by distinguishing "procedural rights" from "substantive rights," which may be conditional but not hypothetical, and proposed that a party's right to adverse costs is not protectable. Given that arbitral hit-and-run concerns are not empirically supported by previous cases but rather rest on a hypothetical scenario, and since there are other measures to filter out unmeritorious claims, this Article concluded that security for costs addresses a hypothetical concern at the cost of investors' real rights to pursue their claims under the ICSID system.

Considering the ICSID Convention's Proposed Rules and its following implications, there is a legitimate concern as to whether the ICSID Convention would still reflect one of the purposes for which it was created: to provide a forum for aggrieved investors to resolve their investment disputes—no matter how poor they are and regardless of whether they are third-party funded.