Overview of current issues for third-party funding in France

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Third-party funding originated in Australia in the early 1990s and primarily developed in common law countries such as the US and UK.

In France, this practice was first recognised in 2006 in a decision of the Versailles Court of Appeal (Société Veolia Propreté c/Foris AG), regarding a financing contract with a third-party paying arbitration costs.

Since this decision, third-party funding has developed in France, but mainly in international arbitration-related matters. Compared to common law countries, however, the practice remains limited given the absence of a specific legislative or regulatory framework. Therefore, only French civil law principles governing commercial contracts apply.

Today, third-party funding is widely recognised as a mechanism for financing litigation by a third party, who pays all of the litigant's bills relating to the trial, in exchange for a percentage of the damages [between 20% and 50%] won at the end of the trial and should not be confused with the funding by the counsel and the application of contingency fees.

In practice, the funder is speculating by anticipating the success of the funded party on the merits of the case. Third-party funding also promotes access to justice for insolvent parties and allows small-sized companies to avoid risking their own funds in expensive arbitration proceedings.

However, practice shows that third-party funding also presents challenges and issues for both the client's counsel (1) and the funder himself (2), which must be addressed by the parties to the dispute as these issues can have a significant impact on the procedure.

Issues to be addressed by counsels

In the relationship between the counsel and the client, the interference of the third-party funder can create what could be called a "ménage à trois". It is then up to lawyers to ensure that their professional and ethical rules are respected.

Obligation of independence and prohibition of conflicts of interest

Considering the risk taken, when financing the procedure, the funder may wish to have a say in the strategy and the conduct of the procedure. However, this interference can present some risks.

But most importantly, the privileged relationship between the counsel and his client must be protected as the third-party funder remains outside of this relationship and does not stand for the counsel's client. This vests in the fact that payment by a third-party funder does not confer the status of client.

The client should in principle be the only one to choose the lawyer and give directions for the conduct of proceedings. But above all, the lawyer will have to keep in mind that the intervention of the funder does not give the latter the status of a client.

In this logic, the third-party funder cannot influence counsels in the litigation strategy (e.g. by threatening to withdraw from the proceedings). Nor should they pressure counsels to refuse a settlement on the grounds that the contractual amount is lower than the amount they invested, while the client would be willing to accept such settlement if he benefits from it.

In terms of fees, French law allows counsels to receive payment from a third person other than their clients. A fortiori, the third-party funder can pay the counsel's fees on behalf of the funded party. Once again, this payment does not make the funder the client.

However, if the President of the Bar (the "bâtonnier") has exclusive jurisdiction for all disputes relating to the payment of lawyers' fees and fee issues between lawyers and clients, they consider themselves incompetent to rule in disputes in which the fees are paid by a third-party funder, thereby depriving counsels of access to justice and of any recourse regarding their fees, which may result in a denial of justice.

Lawyers should therefore pay careful attention to the funding agreements and their terms. One option suggested by the Paris Bar is that the funding agreement expressly grant jurisdiction to the President of the Bar on these issues.

Professional secrecy

One of the main consequences of the funder not being the client is that the lawyer's professional secrecy prevents him from disclosing any information concerning the client or the case to a third-party funder.

Information can only be communicated to the client themself, who remains free to disclose the information they wish to the funder. However, the lawyer should always be careful not to communicate privileged information to the funder directly, therefore avoiding any professional liability.

Duty of transparency of counsels and the disclosure of third-party funding

In principle, French law does not provide for any specific obligation to disclose the existence of a third-party funder in a procedure. However, on 21 February 2017, the Paris Bar Council adopted a resolution recognising the interest of third-party funding and at the same time suggested that counsels representing funded parties advise their clients to disclose the existence of the funding to the arbitral tribunal.

As highlighted in this resolution, the disclosure makes it possible for arbitrators to identify potential conflicts of interests that could result from ties with the funder and therefore prevent the risk of annulment of the award based on a potential lack of independence of the arbitrator.

In this context, the amended ICC rules of 2021 provide for a new Article 11(7) according to which: "each party must promptly inform the Secretariat, the arbitral tribunal and the other parties, of the existence and identity of any non-party which has entered into an arrangement for the funding of claims or defences […]" to ensure the impartiality and independence of arbitrators towards the funded party.

Failure to make such a disclosure can indeed cause an annulment of the award and thus the liability of lawyers.

Therefore, faced with a third-party funder, lawyers should comply with the obligation of transparency, set out in Articles 4.4 and 4.5 of the CCBE Code of Conduct for European Lawyers, by encouraging the client to disclose third-party funding and by warning the client of the consequences of non-disclosure.

Issues for funders

Aside from the investment risk that constitutes third-party funding, funders may face several issues during the procedure, such as the risk of seeing their fee reduced by a judge, the risk of the funding agreement

being annulled or the risk of being considered a party to the proceedings. Yet, these risks remain rather limited in the context of third-party funding in arbitration, and recent court decisions confirm this.

Risk of reduction of the contractually agreed funder's fee if the judge deems it disproportionate

Under article 1165 of the French Civil Code, judges are granted the power to terminate contracts if they deem it necessary, but they also have the power to reduce the contractually agreed funder's fee when it is considered disproportionate.

In 2011, the French Supreme Court ("Cour de cassation") ruled on a dispute between the parties to a funding agreement and considered that when adressing such a dispute the court must verify whether the agreed fee is excessive in light of the service provided by the funder, and if so, the fee should be reduced (case n°10-16.770). In their appreciation, the courts may for instance rely on the scope of the services as well as the duration of the proceedings compared to the percentage of the funder's success fee to reduce it significantly (case n°11/22443) (with the understanding that this case was very fact specific and that the funder was not a professional one).

Therefore, the funder should always pay attention to the amount requested for his intervention and be able to justify it before the judge to avoid any judicial reduction.

Risk of extension of the arbitration agreement to the funder to make it a party to the procedure

In a very recent decision from 25 January 2022, the Paris Court of Appeal (case n°20/12332) received an annulment request of an arbitral award in which, among other things, the arbitral tribunal had considered it had no jurisdiction over the funder. In its decision, the Court refused to consider the third-party funder as a co-claimant to the procedure.

The Court considered that the extension of the arbitration clause to the funder would only be possible in cases of exceptional circumstances, which is the demonstration of an interference that is sufficiently important and above what is reasonably expected from the participation of a funder in a procedure.

According to the Court, the official disclosure of the funder's intervention, the fact that his interest is not only financial or that he was only an occasional funder do not constitute exceptional circumstances.

By doing so, the Court of Appeal sends a positive message to the funders in the context of a French law otherwise keen to extend arbitration clauses to third parties. This decision thus seems to revise the position of the Court of Cassation in the ABS ruling of 2007 (case n°04-20.842), which considered it possible to join third parties to a procedure if they had participated in the negotiation or the performance of the contract.

Considering the absence of any specific legal framework applicable to third-party funding in France, some people have called for more regulation, while others consider that the existing lawyers' professional rules, the provisions of the ICC rules or the principles set out in the IBA rules should be sufficient.

In any event, this matter will continue to raise many questions and issues considering its constant evolution and development in practice.