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Tort liability of arbitrators vis-à-vis third-party arbitration funders in a Danish perspective

This article explores, with reference to Danish law, under which conditions arbitrators might attract a tort liability *vis-à-vis* a third-party arbitration funder who has funded an unsuccessful arbitration. The *lex arbitri* will generally not grant immunity against tort claims, nor will the waiver of liability set out in the rules of procedure of most arbitration institutions grant protection seeing that the funder is not a party in the arbitration and thus not a party in the contractual relationship between the arbitrators and the claimant and the respondent. Danish case law demonstrates that lawyers, in a variety of cases, can be held liable in tort *vis-à-vis* third-parties who suffer a loss as a result of legal malpractice. It is thought, however, that arbitrators will be allowed a considerable margin of error when it comes to deciding a commercial dispute on its merits. That said, where serious procedural errors are made or where it is evident that certain key findings in the award are not in line with the contract or with the applicable law, arbitrators may suddenly find themselves on the receiving end of a tort action brought by a third-party arbitration funder.

Keywords: Third-party arbitration funding, tort liability of arbitrators, immunity, exclusion of liability for arbitrators, duty of care of arbitrators, procedural errors

Table of contents

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I Introduction

In recent years, the landscape of commercial arbitration has witnessed a significant transformation with the emergence and rapid growth of third-party arbitration funders. These entities play a pivotal role in supporting parties involved in high-stake arbitrations by providing the necessary financial backing to pursue their claims by covering the costs associated with legal representation, administrative fees, expert witnesses, and other aspects of dispute resolution against receiving an oftentimes substantial percentage of amounts awarded to the client which is being funded in the arbitration.

The industry of funding major arbitrations has experienced a substantial surge in recent years.[1] More funders have entered the market, offering a variety of funding structures tailored to meet the diverse needs of parties involved in arbitrations. As the demand for arbitration funding grows, funders are adapting to different jurisdictions and legal frameworks, facilitating a global reach for their services. Furthermore, the industry has witnessed increased collaboration and partnerships between law firms, arbitrators, and funders. Law firms are recognizing the value of third-party funding as a tool to expand their client base and undertake more complex cases. This collaboration not only benefits parties seeking funding but also augments the overall efficiency and effectiveness of the arbitration process.

Arbitration funders are not, however, parties to the arbitration, nor do they sign the terms of reference or similar procedural agreements used under the rules of different arbitration institutions.

With reference to Danish law this article explores under which conditions arbitrators may face a tort liability *vis-à-vis* a third-party arbitration funder who has funded an unsuccessful arbitration.

II Arbitrator immunity

Arbitrator immunity is a fundamental principle aimed at protecting arbitrators from personal liability for their actions or decisions made in the course of arbitration proceedings. This immunity encourages individuals to serve as arbitrators without fear of facing legal consequences for honest errors or judgments made during the adjudication process. The concept is enshrined in various arbitration rules: Article 41 of the ICC Rules 2021 stipulates that:

> "The arbitrators, any person appointed by the arbitral tribunal, the emergency arbitrator, the Court and its members, ICC and its employees, and the ICC National Committees and Groups and their employees and representatives shall not be liable to any person for any act or omission in connection with the arbitration, except to the extent such limitation of liability is prohibited by applicable law."

1 The industry has an estimated global value approx. 80bn EUR with more than 100 funders in Europe alone. See in more detail the following article: Insurance Europe, EU should develop rules on third party litigation funding, available at https://www.insuranceeurope.eu/news/2650/eu-should-develop-rules-on-third-party-litigation-funding (12 December 2023).

Similarly, Article 31 para. 1 of the LCIA Rules 2020 dictate that:

> "None of the LCIA (including its officers, members and employees), the LCIA Court (including its President, Vice Presidents, Honorary Vice Presidents, former Vice Presidents and members), the LCIA Board (including any board member), the Registrar (including any deputy Registrar), any arbitrator, any Emergency Arbitrator, any tribunal secretary and any expert to the Arbitral Tribunal shall be liable to any party howsoever for any act or omission in connection with any arbitration, save: (i) where the act or omission is shown by that party to constitute conscious and deliberate wrongdoing committed by the body or person alleged to be liable to that party; or (ii) to the extent that any part of this provision is shown to be prohibited by any applicable law."

Similar rules are found in the rules for the ICDR (Article 38), SIAC (Rule 38), HKIAC (Article 46) and the SCC (Article 52).

However, the immunity provided by these clauses is not absolute and will generally not apply in case of deliberate default or gross negligence that may give rise to liability under the *lex arbitri* (or possibly under the laws of other jurisdictions where damages are incurred as a result of the wrongdoings of an arbitrator). In this vein, there is a noteworthy and fundamental difference in how the common law and civil law approach the topic of immunity.

The common law approach is based on the concept of "judicial immunity" in that judges and arbitrators are perceived as performing, essentially, the same role. Under common law, arbitrators are therefore entitled to an almost unqualified immunity by virtue of their "quasi-judicial" function.[2] This principle is embedded in Section 29 of the English Arbitration Act 1996, which stipulates:

> "An arbitrator is not liable for anything done or omitted in the discharge or purported discharge of his functions as arbitrator unless the act or omission is shown to have been in bad faith".

On the other hand, the UNCITRAL Model Law on International Commercial Arbitration, which has been used as a template for the Arbitration Acts in more than 120 jurisdictions worldwide neither addresses the issue of the liability of arbitrators or their immunity.[3]

The civil law approach to immunity is based on the view that there is a contractual relationship between the parties and the arbitrators and that the parties have agreed to grant the arbitrators immunity from liability under their contract - much like under a commercial agreement excluding a party's liability.[4] However, under most civil law jurisdictions, it is not possible to exclude the liability of a party in case of willful misconduct or gross negligence.[5]

2 Serhii Lashyn, Immunity of Arbitrators, available at https://www.etd.ceu.edu/2019/lashyn_serhii.pdf (12 December 2023).

3 UNCITRAL, Model Law on International Commercial Arbitration, available at https://uncitral.un.org/en/texts/arbitration/modellaw/commercial_arbitration/status (12 December 2023).

4 Agata Cevc, Civil Liability Of Arbitrators, available at https://hrcak.srce.hr/ojs/index.php/eclic/article/download/9009/5097/ (12 December 2023).

5 Tadas Varapnickas, The Law Applicable to Arbitrators' Civil Liability from a European Point of View, available at https://arbitrationblog.kluwerarbitration.com/2019/03/25/the-law-applicable-to-arbitrators-civil-liability-from-a-european-point-of-view/ (12 December 2023).

By way of example, under Dutch law an arbitrator may be held liable for damages in the event of gross negligence without any requirement for the arbitrator to have acted in bad faith.[6]

Similarly, under Swedish law, where the Arbitration Act does not contain any provisions specifically regulating the liability of arbitrators, the prevailing view is that an arbitrator's liability is treated much the same as any other party in a contractual relationship when it comes to assessing the applicability of liability excluding clauses. Accordingly, Article 52 of the SCC Rules (2023)[7] limit the arbitrators' liability "unless an act or omission constitutes wilful misconduct or gross negligence."[8]

Under Danish law and Norwegian law, which have both based their Arbitration Acts on the UNCITRAL Model Law, the position is the same as under Swedish law.

Accordingly, Article 51 of the Rules of Procedure of the Danish Institute of Arbitration stipulates as follows:

> "The members of the Arbitral Tribunal, the secretary of the Arbitral Tribunal, see Article 30, or other persons appointed by the DIA or the Arbitral Tribunal, and the DIA, including the members of the Council of Representatives, the Board, the Chair's Committee, the Secretariat and the Secretary-General shall not be liable for any act or omission in connection with commencement of an arbitration, the processing of an arbitration or an award made by the Arbitral Tribunal, except to the extent such limitation of liability is prohibited by applicable law."[9]

Similarly, Article 37 of the Rules of Arbitration Procedure of the Oslo Chamber of Commerce[10] stipulates:

> "With the exception of losses caused by wilful misconduct or gross negligence, any party that uses the Institute waives any right to assert claims for damages against the Institute, arbitrators or any other person who performs duties for the Institute or who has been appointed to assist the arbitral tribunal."

6 Jonas Angelier/Maartje Verstappen, The Liability Of International Arbitrators: When And Where To Sue?, available at https://www.houthoff.com/expertise/practice/arbitration/arbitration-blogs/the-liability-of-international-arbitrators-when-and-where-to-sue (12 December 2023).

7 SCC, SCC Rules, available at https://sccarbitrationinstitute.se/en/resource-library/rules-and-policies/scc-rules (12 December 2023).

8 Pontus Scherp/Fredrik Norburg/Anina Liebkind, GLI, International Arbitration Laws and Regulations 2023 | Sweden, available at https://www.globallegalinsights.com/practice-areas/international-arbitration-laws-and-regulations/sweden (12 December 2023).

9 A similar rule is found in Article 42 of the Rules of Procedure of the Danish Construction Arbitration Board ("*Voldgiftsnævnet for Byggeri og Anlæg*"), which is the forum for the vast majority of arbitrations in Denmark.

10 Oslo Chamber of Commerce, Rules of the Arbitration and Dispute Resolution Institute of the Oslo Chamber of Commerce, Arbitration and Fast-track Arbitration, available at https://chamber.no/wp-content/uploads/2022/11/OCC_arbitration_rules_2017.pdf (12 December 2023).

III Liability of arbitrators *vis-à-vis* third-party arbitration funders?

As can be seen from the above, under the laws of the Scandinavian countries the immunity of arbitrators is solely based on the articles in the rules of procedure, which apply by virtue of the contract that the arbitrators are seen to have entered into with the parties to the arbitration.

Seeing that there is no direct contractual relationship between the arbitrators and any third-parties funding the arbitration and in the absence of a general immunity protection at law (as the one found in the English Arbitration Act), the arbitrators are not protected against possible claims raised in tort by an arbitration funder who has funded an unsuccessful arbitration.

Accordingly, a third-party arbitration funder may unhindered raise a claim in tort against the arbitrators asserting that they breached their duty of care owed to the funder by failing to perform their duties diligently and competently when they decided the dispute. The fact that the award under the laws of most jurisdictions[11] is final and that it can generally only be set aside where there is evidence of serious procedural errors might enhance the risk of a tort action, (seeing that it is generally not procedurally possible to cure an award which is legally flawed on the merits).

Under the laws of the Scandinavian jurisdictions the requirements for successfully raising a tort claim in this context can briefly be summarized as follows:

1. *Negligence*: To establish whether there is negligence, one will generally have to compare the actual conduct of the arbitrators to the hypothetical conduct of experienced, international arbitrators. Arbitrators are expected to conduct themselves professionally and with a reasonable level of international dispute resolution experience when it comes to resolving procedural issues, interpreting the contract, assessing the evidence and applying the governing law of the contract correctly. In this regard the conduct of the arbitrators can be juxtaposed with the different guidelines on international arbitration issued by the UNCITRAL or the Chartered Institute of Arbitrators (CIArb), when assessing whether the arbitrators have acted negligently. Where the arbitrators have conducted themselves in a manner that deviates from what an experienced international arbitrator would have done, *e.g.*, by basing their findings on evidence or arguments that have not been submitted by either of the parties, they risk being deemed to have acted negligently. In this regard, the case law related to the liability of arbitrators towards the parties for procedural errors may serve as a useful guide when assessing whether a tort liability may come into play.
2. *Proof of loss*: Secondly, a tort liability requires proof that a loss has been incurred. This condition will rarely pose a problem in that the third-party funder will usually have lost its “invested” funds in the dispute in the form of legal costs, expert costs, administrative costs, etc. The more difficult question in this regard is whether the third-party funder can successfully claim loss of

11 With the notable exception of Section 69 of the English Arbitration Act of 1996 which provides parties with the ability to appeal an arbitral award on a point of law.

profits (*i.e.*, loss of the portion of the amount claimed by the funded party in the arbitration that was not awarded).

3. *Causality*: This condition is more challenging as is the case in most tort claims. The third-party funder would have to show that the loss was incurred as a result of the negligence of the arbitrators and that their negligence was a "*conditio sine qua non*", *i.e.*, that the loss would not have occurred "but for" the negligent conduct of the arbitrators.
4. *Foreseeability*: This condition requires the third-party funder to show that it was foreseeable for the arbitrators that their negligence would result in the loss incurred. Where the tribunal has been informed that one of the parties (or both) are being funded by a third-party this condition will rarely present a challenge.
5. *Absence of contributory negligence*: Finally, the third-party funder will likely face challenges where the arbitrators can point to "ineffective representation" by the counsel representing the funded party in the arbitration. Where the counsel has failed to offer substantiated arguments the arbitrators will often be able to exonerate themselves from liability with reference to the fact that their findings were dictated by the manner in which the "case was presented" to them by counsel for the funded party in the arbitration.

The fact that arbitrators may attract liability for gross procedural errors despite the immunity protection embedded in most institutional rules of procedure has been established several times by national courts in both common law and civil law jurisdictions. Errors that may give rise to liability include: Excluding an arbitrator from the deliberation process[12], deciding the case on the basis of evidence or legal arguments that have not been submitted by either party, lack of impartiality and/or independence, an unreasonable or unjustified resignation by an arbitrator, corruption, fraud, forgery, etc.[13]

The more difficult question is whether - and if so under which conditions - arbitrators can be held liable in tort for having failed to correctly apply the governing law of the contract or for having misinterpreted the contract.

The general view under Scandinavian law seems to be that arbitrators will likely be given considerable "wiggle room" when determining whether a failure to correctly decide a case on its merits can give rise to a tort liability, provided of course that the arbitrators have acted in good faith and have complied with the rules of procedure. "Honest mistakes" made in the assessment of the evidence and/or in relation to applying the contract and/or the governing law correctly will therefore only very rarely give rise to a tort liability.[14]

12 Julio Olórtegui, *Puma v. Estudio 2000*: Three Learned Lessons, available at https://arbitrationblog.kluwerarbitration.com/2017/05/29/puma-v-estudio-2000-three-learned-lessons/ (12 December 2023).

13 Papazoglou Stephanie, Jus Mundi, Arbitrator Responsibility, available at https://jusmundi.com/en/document/publication/en-arbitrator-responsibility (12 December 2023).

14 Anders Ørgaard, "*Voldgiftsaftalen*", DJØFs Forlag, København 2006, 45 (with references); See also Niels Schiersing, "Voldgiftslov med Kommentarer", DJØFs Forlag, København 2016, 249 et seq (with several references).

IV Case law

The available reported case law on the issue of tort liability of arbitrators is scarce, however, some guidance may be found for example in tort cases where a lawyer has prepared a testament for a client designed to ensure that a certain beneficiary receives a certain portion of the probate estate of the client. Where the testament fails to meet this goal, the lawyer may face a claim in tort raised by the disgruntled beneficiary.

In the Danish case, UfR 2008.1324 V[15], a lawyer was thus held liable in tort for the loss suffered by a foundation, which had been established in connection with a testament drafted by the lawyer. It had been a clear prerequisite for the testator that the foundation would be tax exempt, which turned out not to be the case.[16]

Another group of cases concerns the tort liability of lawyers *vis-à-vis* buyers of real estate. In the Danish case, UfR 2010.2375 H[17], the lawyer represented the seller of an apartment. The lawyer failed to observe the rules on the maximum price that could be demanded for the apartment as regulated in the Danish Cooperative Housing Association Act, and consequently the buyer of the apartment suffered a loss when he resold the property at a lower price (as allowed by said Act). The Supreme Court found that the lawyer should have informed both his client (the seller) and the buyer that the transaction was governed by the special rules set out in the mentioned Act. The lawyer was thus held liable for damages and was ordered to pay compensation to the buyer for the incurred loss.

Finally, a lawyer may attract a tort liability *vis-à-vis* the tax authorities. In UfR 2000.365/2 H[18], (often referred to as the "*Thrane Case*") a company in which there were only liquid assets and a tax debt, was sold at an inflated price after the business had ceased. The sale was assisted by the seller's lawyer, by an accountant and by the buyer's bank. It was agreed between the parties that the purchase price would be transferred from the buyer's bank to the seller's bank and that the company's funds would be transferred to the buyer's bank on the same day. This emptied the company of funds without any tax being paid. In their assessment of the lawyer's liability, the Danish Supreme Court emphasized that the transfer was not a normal business transaction. Therefore, the advisors should have been aware of the risk that the tax authorities could suffer a loss. The seller's lawyer was therefore held liable for the tax authorities' loss.

15 Judgment UfR 2008.1324 V, rendered by the Western Division of the Danish High Court ("*Vestre Landsret*") printed in the Danish Weekly Law Reporter Vol 2008, 1324 et seq.

16 See also the similar decision FED 2008.235 V concerning errors made by a lawyer in relation to a prenuptial agreement. The judgment, which was rendered by the Western Division of the Danish High Court is printed in the journal, "Forsikrings- og Erstatningsretlig Domssamling" Vol 2008, 235 et seq.

17 Judgment rendered by the Danish Supreme Court ("*Højesteret*") printed in the Danish Weekly Law Reporter Vol 2010, 2375 et seq.

18 Judgment rendered by the Danish Supreme Court printed in the Danish Weekly Law Reporter Vol 2000, 365 et seq.

The *Thrane Case* has attracted renewed interest and attention in recent years due to the "dividend washing" scandal, which a number of major law firms across Europe have been involved in and have subsequently been sued for in tort by among others the Danish tax authorities. One particular case should be mentioned in this context as it may serve to illustrate the extent of the duty of care, which lawyers are deemed to have towards third parties:

On 2 November 2023, the Danish Supreme Court ordered one of Denmark's largest law firms, *Bech-Bruun*, to pay more than ½ billion DKK (including interest) in tort damages to the Danish tax authorities.[19] The case, which was initiated in April 2020 in the Eastern Division of the Danish High Court, arose out of a tax opinion prepared by *Bech-Bruun* in 2014 for the German bank, the North Channel Bank. In the tax opinion, *Bech-Bruun* gave advice on how the bank could participate as a depository bank in so-called "*cum-ex*" transactions, also known as "dividend washing", involving *double* refunds of dividend withholding tax – in other words, tax fraud.

In its judgment the Supreme Court among other things held that *Bech-Bruun's* tax lawyer who had prepared the tax opinion "had to realize that there was an obvious risk that North Channel Bank, together with others, was involved in preparing a model for unjustified refunds of dividend tax." In this connection the Supreme Court emphasized that the lawyer in an e-mail from the bank's German lawyers had been "made aware of the risk of double refund of dividend tax" and that he therefore had "to be aware of the risk of setting aside the interests of the tax authorities". Further, the Supreme Court emphasized that the lawyer had found himself in "an elevated responsibility risk environment" as the envisaged "cum-ex" transactions appeared to have no commercial justification.

Danish case law (and in particular the "*Bech-Bruun* case") clearly demonstrates that lawyers in a variety of cases can be held liable in tort *vis-à-vis* third-parties who suffer a loss as a result legal services provided to a client. In the context of dispute resolution services, it is thought, however, that arbitrators will be allowed a considerable margin of error when it comes to deciding a commercial dispute on its merits. That said, where procedural errors are made or where it is evident that certain key findings in the award are not in line with the contract or with the applicable law, arbitrators may suddenly find themselves "on the other side of the bench" facing an uncomfortable degree of scrutiny in a tort action brought by a financially strong arbitration funder with substantial litigation experience.

V Conclusion

Historically, funding large-scale arbitrations often posed financial challenges for parties seeking redress through the arbitration process. The costs associated with legal representation, administrative fees, expert witnesses, and other aspects of dispute resolution can be substantial. Recognizing this gap, third-party arbitration funders have stepped in to bridge the financial divide and level

19 A transcript of the judgment is available at https://domstol.dk/media/apsbobj0/20331-2022-anonym-dom.pdf (12 December 2023).

the playing field, enabling parties to pursue their claims without being hindered by financial constraints.

The use of third-party arbitration funding has increased dramatically over the recent years and is today a multi-billion Euro industry. Arbitration funders conduct a thorough due diligence of each case with legal opinions and expert assessments in order to determine the risks involved before deciding to fund a party. In light of the considerable investments made by funders in major commercial disputes it is not unlikely that they will explore the possibility of raising claims against both counsels and arbitrators (or their insurance companies) where a funded case is lost.

International arbitrators should be aware of this risk, in particular since the *lex arbitri* will generally not grant immunity and since the waiver of liability set out in the rules of procedure of most arbitration institutions will not protect arbitrators against tort claims raised by a third-party arbitration funder given the fact they the funder is not a party in the arbitration and thus not a party in the contractual relationship between the arbitrators and the claimant and the respondent.

[redacted] Moreover, arbitrators acting in *ad hoc* arbitrations[20] should verify whether their professional indemnity insurance policies provide adequate cover both in terms of limits and in terms of scope. In this connection it is worth mentioning that some policies afford only limited cover or no cover at all for legal work involving foreign law.

Finally, the large arbitration institutions could consider expanding the usual immunity protection set out in their procedural rules, for example with a provision whereby a funded party undertakes to hold harmless, indemnify and protect the arbitrators from and against tort claims raised by that party's third-party arbitration funder.

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