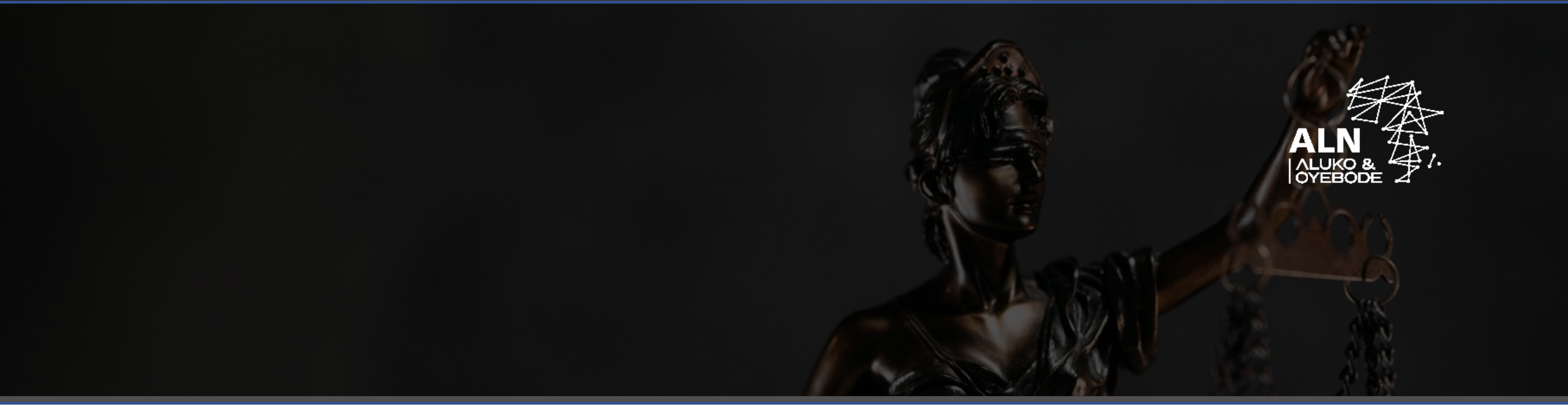

Third-Party Funding of Arbitrations Seated in Nigeria: Key Considerations for Funders

Introduction

One of the key introductions of the Arbitration and Mediation Act, 2023 (AMA) is the provision for Third Party Funding (TPF) of arbitrations seated in Nigeria and arbitration-related proceedings in any court in Nigeria. This represents a significant development considering that previously, the common law principle against maintenance and champerty prevailed in Nigeria. Under the new regime, the twin torts of maintenance and champerty have been abolished. This ensures that the Third-Party Funder gets the protection of the law when enforcing in Nigeria, the Third-Party Funding Agreement (TPFA) or a foreign award arising from such agreement. It also paves the way for the Arbitral Tribunal, when fixing the costs of arbitration in its award, to consider the costs of obtaining third-party funding.[1] This article articulates the essential features of TPF under the AMA and highlights the key considerations for persons who desire to enter third-party funding arrangements.

Features of Third-Party Funding Under the AMA

The AMA represents a shift in the legal treatment of TPF of arbitrations and arbitration-related proceedings in any court in Nigeria. The key features of TPF under the AMA are:

1) The Third-Party Funder may be a natural or legal person.[2]

2) The Third-Party Funder may enter the agreement either with a disputing party, an affiliate of that party, or a law firm representing that party.[3] However, considering the principle of privity of contract, which still applies in its raw form in Nigeria, care must be taken while deciding who the counterparty is in the funding agreement or in what capacity a non-disputing party enters the agreement with the funder. Where the funder expects the disputing party to reimburse the funding cost or make any payment from any successful award, then it is important that the disputing party is a party to the funding agreement or that the non-disputing party enters the agreement as an agent of the disputing party. Otherwise, the funder cannot sue the disputing party under the agreement even if the latter derives benefit therefrom.

3) The funding may be for the arbitration seated in Nigeria or arbitration-related proceedings in any court in Nigeria.[4] The AMA provides for the extent of the Court's intervention in arbitration.[5] Where proceedings are pending in court that are related to arbitration, for example, in respect of the appointment of the arbitrator where a party defaults, securing interim measures, enforcement of the award, setting aside the award, etc., the funding agreement may extend to or exclusively cover the cost of such proceedings.

4) The Third-Party Funder may finance part or all of the cost of the proceedings, either individually or as part of a selected range of cases.[6]

[1] Section 51(1)(h) of AMA. However, the AMA says nothing about the power of the Court to consider the TPF when fixing cost in arbitration related court proceedings. In the absence of such provision, our view is that this will be treated the same way that the court treats cost under its rules.
[2] Section 91 AMA.
[3] Ibid.
[4] Ibid.
[5] Section 64(1) of the AMA.
[6] Ibid.

5) The financing may be provided either through a donation or grant or in return for reimbursement dependent on the outcome of the dispute or in return for a premium payment.[7] This means that the funding may be done for charity or for profit.

6) The TPF is usually executed through a TPFA.[8]

7) **Exemption from Maintenance and Champerty:** The Act expressly provides that the torts of maintenance and champerty do not apply to third-party funding of arbitration.[9]

8) **Disclosure Requirements:** The Act mandates the benefiting party to give written notice of the identity and contact details of funders to the arbitral tribunal, other parties, and relevant arbitral institutions. This aims to prevent conflicts of interest and ensure that all the parties are aware of potential influences on the arbitration process.[10] The disclosure requirement applies to TPFA that came into force on or before the commencement of the arbitration, or after the commencement of the arbitration. The written notice shall be given without delay as soon as the funding agreement is made.[11]

7) **Security for Cost:** The Act codifies the arbitral tribunal's authority to award security for costs against the funded party. Thus, where a respondent has brought an application for security for cost based on the disclosure of third-party funding, the arbitral tribunal may allow the funded party or its counsel to provide the tribunal with an affidavit stating whether under the TPFA, the funder has agreed to cover adverse costs. The affidavit so provided shall be a relevant consideration in the decision of the tribunal on whether to grant security for costs.[12]

8) **Legal Costs and Fees in obtaining Third-Party Funding:** In arbitration proceedings, the tribunal is responsible for determining the overall costs associated with the arbitration in its final award.[13] The Act allows the costs associated with obtaining such third-party funding to be included in the overall arbitration costs, provided they are approved by the tribunal. By recognizing the cost of obtaining third-party funding in cost assessments, the tribunal ensures a fair approach to balancing the financial responsibilities of both parties while promoting access to justice.

Key Considerations for Funders

TPF offers strategic opportunities for both investors and charity financiers. However, if either of these groups is to take advantage of this unique opportunity, they must tread cautiously to successfully navigate this landscape or at the very least, do so with minimal risk. Here are some key considerations:

1) **Conflict Checks:** It is essential to perform a thorough conflict check on both the funded party and any opposing parties in the dispute. Additionally, understanding the nature of the underlying dispute is crucial for identifying and mitigating potential conflicts from the funding arrangement, ensuring all parties adhere to ethical and legal standards.

2) **Risk Assessment and Management:** Risk assessment and management are critical components for the funder when considering the financial and reputational implications of funding arbitration cases. The funder must assess reputational risks, particularly how involvement in a specific case might affect its standing in the industry and with stakeholders. It is important to consider how the arrangement may impair other transactions or relationships in which the funder may be involved.

[7] Ibid.
[8] Ibid.
[9] Section 61 AMA.
[10] Section 62 AMA.
[11] Section 62(2)(a)(b) AMA.
[12] Section 62(3) AMA.
[13] Section 50(1) AMA.

3) **Case Due Diligence:** The funder must conduct due diligence to evaluate the case by assessing both the legal and factual strengths of the dispute. This involves analysing relevant laws and evidence, identifying potential challenges, and examining the credibility of all parties involved. This process will invariably entail the use of legal experts who are knowledgeable in the chosen law governing the dispute.

4) **Capacity of Funded Party:** When the funded party is an entity, it is vital to evaluate its capacity to receive funding by reviewing its Memorandum and Articles of Association. This ensures the entity has the legal authority to enter a funding agreement. It is also important to check if further authorization from the board of directors or shareholders is necessary, as this ensures compliance with corporate governance and reduces potential legal issues related to the funding.

5) **Funding Agreement Structure:** The TPFA should clearly outline the terms of the funding agreement, including the amount, repayment terms, moratorium, and the funder's share of any recovery whether as a percentage of the award, a fixed fee, or a hybrid approach, while considering currency exchange risks.

6) **Managing Confidentiality:** To effectively manage confidentiality, there is need to establish robust confidentiality provisions to safeguard sensitive information pertaining to both the arbitration and the funding agreements. By doing so, the funder can protect proprietary data and maintain the trust of all involved, thereby fostering a secure and transparent environment for the arbitration proceedings.

7) **Dispute resolution:** Funders must carefully evaluate the dispute resolution mechanism they desire to include in the TPFA and ensure that it is fit for purpose.

8) **Priority of Interest:** This determines the order in which claims or interests will be satisfied if the arbitration results in a favourable outcome. Funders who provide financial support with an eye for profit, must carefully evaluate the underlying contract, security agreements, and subordination agreements to identify any potential conflicts or issues related to priority. This includes understanding the hierarchy of claims, such as secured claims, statutory priorities, and contractual provisions.

9) **Non-Disclosure Agreement (NDA):** It is advisable for third-party funders to be aware of any existing NDAs between the parties to the dispute and to ensure that the funders have the necessary consent or carve-outs in place before receiving any confidential information. This can help to protect the funder's interests and avoid potential legal disputes.

10) **Tax Implications:** Funders in a third-party transaction must take special heed to the tax implications as it relates to their investment. Local funders and foreign funders alike who are investing in Nigeria are generally subject to local tax laws. However, the specific tax implications can vary depending on the nature of the investment, the type of entity/person involved, and any applicable tax treaty. Key tax considerations will be highlighted from a local and foreign funder's perspective:

    a) **Local Funder**

    Individual funders may be subject to personal income tax on income earned from their funding activities. The income will be taxed at the applicable rate after deducting allowable expenses. Corporate funders might be subject to a 30% company income tax, or less if they qualify for certain exemptions, depending on their status.

    b) **Foreign Funders**

    The tax implications for foreign funders investing in arbitration in Nigeria are contingent upon the specific circumstances of the funding arrangement and the foreign funder's tax residency. Thus, the tax treatment will depend on whether the funder is a non-resident or individual entity.

Generally, a non-resident funder, whether an individual or a corporation, will be subject to Nigerian income tax only on income derived from Nigeria except where the investment is made from a treaty country in which case, the Funder may enjoy favourable or preferential tax treatment.

11) **Monitoring and Reporting:** Monitoring and reporting are essential in third-party funding of arbitration, allowing funders to track the case's progress and evaluate their investment's effectiveness. However, this requires the funded party to obtain consent to share information about the proceedings with the funder. Implementing processes for ongoing case monitoring ensures funders receive timely updates on key developments, helping them identify potential challenges and opportunities.

12) **Inflow of capital:** Foreign funders involved in cross-border financing must comply with the Central Bank of Nigeria's (CBN) Regulations regarding foreign currency borrowings. Key legislation affecting this area includes the Foreign Exchange (Monitoring & Miscellaneous Provisions) Act (FEMM Act) which established the foreign exchange market and the certificate of capital importation regime for foreign loans. The FEMM Act allows a third-party funder to inflow capital using foreign currency as long as it is done through an Authorised Dealer. When the third-party funder brings in capital and converts it to Naira, it may obtain a Certificate of Capital Importation (CCI) from the bank. The CCI confirms the amount of foreign capital brought into Nigeria, its Naira equivalent, and the names of both the funder and the funded. With this CCI, the funder can access the foreign exchange market to buy foreign currency at the official rate, allowing them to repatriate the investment's principal and interest payments.[14]

13) **Repatriation of Funder's Fund:** Repatriation is a critical consideration for third-party foreign funders involved in arbitration because it directly impacts the realization of returns on their investments. In Nigeria, foreign funders can facilitate repatriation by inflowing money through official channels and obtaining a CCI.

14) **Exit Strategy:** Foreign funders should establish a well-defined exit strategy to address the potential risks of political instability, legal uncertainties, and challenges in enforcing arbitration awards. Funders who wish to exit their investment before the anticipated return or at any stage of the arbitration process can structure their agreements to include options like assignment, novation, or other exit mechanisms.

Conclusion

Third-party funding of arbitration seated in Nigeria and arbitration related proceedings in any court in Nigeria represents a notable development in Nigeria. While it unlocks essential resources to parties, thereby guaranteeing greater access to justice, it also creates a veritable opportunity for an investment that is backed by law. For persons looking to enter such financial arrangements, it is crucial to bear in mind key considerations including risk assessment, confidentiality, inflow of capital, priority of interests, case monitoring, exit strategy, repatriation of funds, tax implications, etc. Such considerations will help minimise risk, enhance the viability of the investment and ensure compliance with local laws.

[14] Section 15 FEMM Act.

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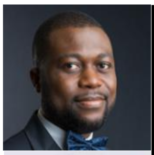

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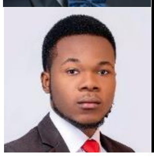

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