ABUSIVE CONDUCT IN INVESTOR-STATE ARBITRATION: A FOCUS ON FRIVOLOUS CLAIMS

Yatırımcı-Devlet Tahkiminde Suistimal Niteliğindeki Eylemler: Mesnetsiz İddialara Bakış

Dr. M. Üzeyir KARABIYIK*

Abstract: The structural deficiencies of the investor-state dispute settlement (ISDS) system pave the way for foreign investors' abusive conduct. As one of the most frequently faced forms of abusive conduct, the use of frivolous claims has become a growing concern. Despite lacking legal merit, frivolous claims can generate damaging consequences for host states. This article first discusses the characteristics of frivolous claims in ISDS practice through examples from arbitral case law. It subsequently examines the existing tools and mechanisms that can be employed to cope with this phenomenon, focusing primarily on early dismissal mechanisms in institutional rules and investment treaties and security for costs. Finally, the efficacy of third-party funding in curtailing frivolous claims is addressed.

Keywords: ISDS, investor-state arbitration, frivolous claims, security for costs, third-party funding, early dismissal mechanisms

Öz: Yatırımcı-devlet uyuşmazlık çözümü (ISDS) sistemindeki yapısal eksiklikler yabancı yatırımcıların suistimal niteliği taşıyan eylem-lerinin önünü açmaktadır. En sık rastlanan suistimal niteliğindeki ey-lemlerden olan mesnetsiz iddialara başvurma büyüyen bir kaygı haline gelmiştir. He ne kadar hukuki dayanaktan yoksun olsalar da mesnetsiz iddialar ev sahibi devletler açısından zararlı sonuçlara yol açabilmektedir. Bu makale ilk olarak ISDS uygulamasındaki mesnetsiz iddiaların özelliklerini tahkim içtihadından örnekler kullanmak suretiyle incelemektedir. Akabinde bu olgu ile mücadelede kul-lanılabilecek araç ve mekaniz-maları öncelikle kurumsal ku-rallardaki ve uluslararası yatırım anlaşmala-rındaki erken ret mekanizmalarını ve masraflar için garanti uygula-masını ele almak suretiyle değerlendirmektedir. Makalede son olarak üçüncü taraf finansmanının mesnetsiz iddiaları engellemedeki etkisine değinilmiştir.

Anahtar kelimeler: ISDS, yatırımcı-devlet tahkimi, mesnetsiz iddialar, masraflar için garanti, üçüncü taraf finansmanı, erken ret mekanizmaları

* Judge, Presidency of the Republic of Türkiye, uzeyirkarabiyik@hotmail.com, ORCID:0000-0002-4806-0673

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INTRODUCTION

Frivolous claims are the claims that lack legal merit. This lack manifests itself in various ways including lack of a basis to establish jurisdiction and inadequacy of legal arguments. Although lacking palpable legal merit, frivolous claims are still able to harm respondent states.[1] They also impair the efficiency of the investor-state dispute settlement (ISDS) system.[2] Since these claims are deprived of legal merit, they could be easily crafted by investors who seek to abuse the system.[3] A United Nations Conference on Trade and Development (UNCTAD) note frames these concerns:

"The significant increase in investment disputes over the last decade has given rise to the concern that investors may abuse the system. Investors may be eager to claim as many violations of the applicable IIA as possible in order to increase their chances of success. This may take a heavy toll in terms of time, effort, fees and other costs, not only for the parties to the dispute, but also for the arbitral tribunal. It is within this context that several countries have advocated a procedure to avoid 'frivolous claims' in investment-related disputes, namely claims that evidently lack a sound legal basis."[4]

Determining whether a claim is frivolous typically necessitates a case-by-case evaluation. If the claim is originated from a violation of a settled rule, this evaluation process would be relatively straightforward for arbitrators. Nonetheless, imprecise standards reign in investor-state arbitration procedures, which complicates an arbitrator's task to determine if a claim truly lacks legal merit. This complication, beyond doubt, creates a fertile ground for unscrupulous investors who are disposed to exploit the arbitration process.

I. FRIVOLOUS CLAIMS IN INVESTOR-STATE ARBITRATION IN A NUTSHELL

Identifying frivolous claims in ISDS settings poses some difficulties due to various reasons. First, instead of periodically receiving a predetermined salary, arbitrators are generally paid per hour or per

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1 Tsai-Fang Chen, Deterring Frivolous Challenges in Investor-State Dispute Settlement, 8 Contemp. Asia Arb. J. 61 (2015), at 65. The harm could be in the form of, among others, unduly delays and costs, reputational harm and regulatory chill.

2 Id.

3 Id.

4 UNCTAD, 'Investor–State Dispute Settlement and Impact on Investment Rulemaking' (UNCTAD/ITE/ IIA/2007/3), at 82, available at: https://unctad.org/en/Docs/iteiia20073_en.pdf, (last accessed 20 February 2019).

case.[5] This form of remuneration might entice arbitrators to exercise their discretion to interpret the "frivolousness" of the claims in their best interests and proceed with them as if they have satisfactory legal merit.[6] In so doing, they ensure the continuity of their remuneration, which is commensurate with the time they spend on the case. Second, arbitrators are not bound by the way the states interpret investment treaties. Therefore, there is always a possibility that arbitral tribunals' interpretations of a treaty provision are at variance with the intent of the states that drafted the said provision.[7] Simply put, a claim may be frivolous in the eyes of the states, while tribunals may think otherwise. Third, since there is no binding precedent or appeal practice in investor-state arbitration, a rejected claim due to lack of legal merit may be raised again without being barred.[8] All these grounds hand the opportunity of bringing frivolous cases to investors on a silver platter.

The international investment arbitration system was designed to resolve disputes between host states and foreign investors. The power of arbitral tribunals in this system has its source in the agreement based on parties' intent to arbitrate, in other words, intent to resolve disputes. In recent years, as a reflection of ever-increasing litigiousness within the investor-state arbitration system, investors have developed a tendency to resort to arbitration for purposes other than having their disputes resolved.[9] The purposes of bringing these types of frivolous claims involve, among others, intervening in criminal proceedings in the host state, gaining media attention, and compelling the state to settle.

To illustrate, in the *Rompetrol* case, the claimant initiated ICSID arbitration in 2005 by claiming, among other things, that Romanian authorities' criminal investigations, detention and wire-tapping of its directors were politically motivated and amounted to a violation of the Netherlands-Romania BIT.[10] In response, the respondent argued that the sole purpose of the claimant in commencing arbitration was to put pressure on Romania to force it to terminate pending criminal

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5 Brooke Guven/Lisa Johnson, The Policy Implications of Third-Party Funding in Investor-State Dispute Settlement, Columbia Center on Sustainable Investment, CCSI Working Paper (2019), at 22.

6 M. Üzeyir Karabıyık, Investor Misconduct in International Investment Arbitration: Can the Unclean Hands Doctrine be a Cure?, Year: 12, Issue: 22, July 2021, Law & Justice Review, at 213.

7 Guven, supra note 5, at 21.

8 Guven, supra note 5, at 22.

9 Emmanuel Gaillard, "Abuse of Process in International Arbitration", 2017, ICSID Review, pp. 1–22, at 10.

10 Rompetrol Group N.V. v. Romania, ICSID Case No. ARB/06/3, Award, 6 May 2013.

proceedings against the managers of the Rompetrol group of companies.[11] The respondent added that the criminal investigations in question were carried out legitimately as per the National Anti-Corruption Strategy. The tribunal noted that the criminal investigations were against the individuals who were linked to the investment, not against the investment itself. In the tribunal's view, to be able to substantiate its claims regarding the BIT violation, the claimant needed to demonstrate the link between the criminal investigations against the individuals in question and the government's conduct against the investment, even if these investigations were unlawful and violated the investigated individuals' personal rights.[12]

Similarly, the tribunal accepted that domestic criminal investigations might amount to a BIT violation if they are severe enough to affect the investor's interest and if the state failed to pay adequate attention to how to protect these interests properly.[13] On the other hand, the tribunal made it clear that association with a foreign investment can not render individuals immune from domestic criminal proceedings.[14] In later stages of the proceedings, the respondent withdrew its objection to the claimant's statement that indicated that it challenged the way the criminal proceedings were conducted, not the criminal proceedings themselves.

The *Rompetrol* award draws attention to the paucity of arbitral case law on how to strike a balance between the legitimate interests of the host states and those of foreign investors in the event of an ongoing domestic criminal investigation that might adversely affect the investment.[15] The tribunal tried to strike this balance by laying down conditions and determinations that would be a useful guide for other arbitral tribunals given that this trend of challenging domestic criminal investigations through invoking investment treaty protections is becoming increasingly popular among investors.

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[11] Id.; Gaillard, supra note 9, at 11.

[12] Rompetrol, Award, supra note 10, 151.

[13] Id. 278. The tribunal noted: "Likewise, in this Tribunal's view, a State may incur international responsibility for breaching its obligation under an investment treaty to accord fair and equitable treatment to a protected investor by a pattern of wrongful conduct during the course of a criminal investigation or prosecution, even where the investigation and prosecution are not themselves wrongful. The provisos are however that the pattern must be sufficiently serious and persistent, that the interests of the investor must be affected, and that there is a failure in these circumstances to pay adequate regard to how those interests ought to be duly protected."

[14] Id. 152.

[15] Id.

Although it was not an investor-state arbitration, the recent ICC case between EDF International S.A.S. and Neckarpri GmbH (owned by the German federal state of Baden-Württemberg) could be another example of a frivolous claim the sole purpose of which was gaining media attention.[16] Professor Gaillard who represented EDF International S.A.S. in this case noted in his article:

"Following the nuclear disaster in Fukushima, a newly-elected coalition government in Baden-Wurttemberg (which included members of the Green Party) brought a claim against EDF, arguing that it had overpaid EDF for shares in a local nuclear power company. The clear motive behind the claim was to demonstrate that the previous administration in Baden-Wurttemberg was misguided in purchasing EDF's shares in the company immediately before the Fukushima events, which had a dramatic impact on their value. Baden-Wurttemberg's goal of gaining publicity was made amply clear when it televised an expert report concerning the value of the shares six months before the report was even submitted to the arbitral tribunal."[17]

The concept "claims manifestly without legal merit" also involves the frivolous claims the subject of which clearly falls outside of the jurisdiction of the tribunal.[18] In *Emmis et al. v. Hungary*, since the jurisdiction of the tribunal was limited to claims of expropriation, the tribunal held that all non-expropriation claims were outside the scope of its jurisdiction and had accordingly no legal merits.[19] The tribunal in the case *Brandes v. Venezuela* shared a similar viewpoint.[20] The claimant brought the claims asserting that Venezuela violated its fair and equitable treatment obligation and expropriated the investment without compensation. Challenging the jurisdiction of the tribunal, Venezuela alleged that the claims were manifestly without legal merit and needed to be expeditiously dismissed under Rule 41(5) of the ICSID Arbitration Rules. In its decision on the respondent's preliminary objection the tribunal noted: "The Tribunal first of all notes that Rule 41(5) does not mention 'jurisdiction.' The terms employed are 'legal merit.' This wording, by itself, does not provide a reason why the question whether

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16 ICC Case No 1815/GFG/FS, Award 6 May 2016.; Gaillard, supra note 9, at 10.

17 Gaillard, supra note 9, at 10.

18 Chen, supra note 1, at 65.

19 Emmis et al. v. Hungary, ICSID Case No. ARB/12/2, Decision on Respondent's Objection Under ICSID Arbitration Rule 41(5), 11 March 2013, 65, 85; See also Chen, supra note 1, at 65.

20 Brandes Investment Partners, LP v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/08/3, Decision on the Respondent's Objection Under Rule 41(5) of the ICSID Arbitration Rules, 2 February 2009.

or not a tribunal has jurisdiction and is competent to hear and decide a claim could not be included in the very general notion that the claim filed is 'without legal merit.'"[21] Consequently, the tribunal rejected the respondent's jurisdictional objection.

Claims that are not pertinent to the investments as defined by Article 25 of the ICSID Convention would be without legal merits and can also be deemed frivolous. In *Global Trading v. Ukraine*, the tribunal noted: "the Tribunal considers that the purchase and sale contracts entered into by the Claimants were pure commercial transactions and therefore cannot qualify as an investment for the purposes of Article 25 of the Convention."[22]

II. REMEDYING FRIVOLOUS CLAIMS

Facing an investment arbitration claim could be quite frustrating for host states, mainly due to the initial financial burden originating from legal representation and procedure-related expenses. The average cost for a respondent state in an investor-state arbitration is around USD 5 million.[23] Even if the claim has no legal merit and the investor has no real chance to prevail, the respondent state would have to allocate a sizable amount of financial resources to its defense. Particularly, states with relatively weak economies would not be very enthusiastic about such an allocation. Moreover, as opposed to host states, the practice of third-party funding comes into view as a practical and risk-mitigating tool for investors. This unfair state of affairs equips the investors with the opportunity to resort to the tactic of initiating unmeritorious claims to gain leverage in their conflict resolution negotiations with host states. Apart from the remedies of general character above-mentioned, two specific tools shine out in deterring frivolous claims: early dismissal mechanisms and security for costs.

A. EARLY DISMISSAL MECHANISMS

States' ever-mounting discomfort with frivolous claims and concomitant financial and time-wise burdens have necessitated tackling the issue at the level of arbitral institutions. In parallel with the augmentation in the number of international investment arbitration

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[21] Id. 50.

[22] Global Trading Resources Corp. & Globex International Inc. v. Ukraine, ICSID Case No. ARB/09/11, Award, 1 December 2010, ¶ 56.

[23] International Council for Commercial Arbitration (ICCA), Report of the ICCA-Queen Mary Task Force on Third-party-funding in International Arbitration, The ICCA Reports No.4, April 2018, Annex C, at 244. (Hereinafter ICCA-QM Report)

claims lodged, states' complaints regarding the ICSID Secretariat's insufficiency in weeding out the claims lacking legal merit have grown apace over time.[24] Article 36(3) of the ICSID convention authorizes the Secretary-General of ICSID to screen the requests for arbitration and not register a claim if the dispute is manifestly outside of the center's jurisdiction.[25] Nevertheless, the said authority of the Secretary-General is inadequate when it comes to eliminating unmeritorious claims, as it does not allow a screening regarding the merits of a dispute.[26] Likewise, the Secretary-General would have to register the arbitration requests if the center's jurisdiction was not manifestly lacking, even if it was doubtful.[27]

After engaging in consultations with various interest groups and stakeholders in 2005, the ICSID Secretariat drafted a new rule that formulated an early dismissal mechanism for the claims manifestly lacking legal merit. Rule 41(5) reads:

"Unless the parties have agreed to another expedited procedure for making preliminary objections, a party may, no later than 30 days after the constitution of the Tribunal, and in any event before the first session of the Tribunal, file an objection that a claim is manifestly without legal merit. The party shall specify as precisely as possible the basis for the objection. The Tribunal, after giving the parties the opportunity to present their observations on the objection, shall, at its first session or promptly thereafter, notify the parties of its decision on the objection. The decision of the Tribunal shall be without prejudice to

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[24] Alvin Yeo/Koh Swee Yen, Objection of Manifest Lack of Legal Merit of Claims: Arbitration Rule 41(5), The Investment Treaty Arbitration Review, 4th Edition, 2019, at 60.

[25] Convention on the Settlement of Investment Disputes between States and Nationals of Other States, Article 36(3). The article reads: "The Secretary-General shall register the request unless he finds, on the basis of the information contained in the request, that the dispute is manifestly outside the jurisdiction of the Centre. He shall forth- with notify the parties of registration or refusal to register."

[26] ICSID Secretariat, Working Paper on 'Suggested Changes to the ICSID Rules and Regulations', 12 May 2005, at 7. The relevant paragraph of the paper reads: "Secretary-General's power to screen requests for arbitration does not extend to the merits of the dispute or to cases where jurisdiction is merely doubtful but not manifestly lacking. In such cases, the request for arbitration must be registered and the parties invited to proceed to constitute the arbitral tribunal.", available at:

https://icsid.worldbank.org/en/Documents/resources/Suggested%20Changes%20to%20the%20ICSID%20Rules%20and%20Regulations.pdf (last accessed 15 January 2022)

[27] Id.

the right of a party to file an objection pursuant to paragraph (1) or to object, in the course of the proceeding, that a claim lacks legal merit."[28]

Trans-Global v. Jordan, is the first case in which Rule 41(5) was invoked.[29] The claimant, Trans-Global Petroleum Inc., asserted that the host state failed to provide fair and equitable treatment of the investment and impaired the investment through discriminatory measures.[30] The claimant initiated ICSID proceedings and asserted that once it discovered the oil pay zones, the respondent "began a systematic campaign to destroy the Claimant's investment by preventing the Claimant from pursuing any further role in the development of those oil deposits."[31] To Trans-Global, the respondent state violated the U.S.-Jordan BIT provisions on fair and equitable treatment, non-discrimination and the obligation to consult the claimant.[32] The respondent countered these claims with invoking Rule 41(5).[33] It asserted that the allegedly infringed legal rights and obligations in the claim were non-existent, and therefore, the claim manifestly lacked legal merit.[34] After having discussed the term "manifestly without legal merit" in detail[35], the tribunal opined that the first two violations asserted by the

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[28] ICSID Rules of Procedure for Arbitration Proceedings, Rule 41(5) came into effect on 10 April 2006. Rule 45(6) of the ICSID Additional Facility Rules also contains the same text.

[29] Trans-Global Petroleum, Inc. v. Hashemite Kingdom of Jordan, ICSID Case No. ARB/07/25, Decision on the Respondent's Objection Under Rule 41(5) of the ICSID Arbitration Rules, 12 May 2008.

[30] Id. 16.

[31] Id. 12.

[32] Id. 15-16.

[33] Id. 19.

[34] Id. 95.

[35] Id. 93-105. The following determinations of the tribunal is noteworthy: "The Tribunal considers that the adjective "legal" in Rule 41(5) is clearly used in contradistinction to "factual" given the drafting genesis of Rule 41(5)... Accordingly, it would seem that the tribunal is not concerned, per se, with the factual merits of the Claimant's three claims. At this early stage of these proceedings, without any sufficient evidence, the Tribunal is in no position to decide disputed facts alleged by either side in a summary procedure. Nonetheless, the Tribunal recognises that it is rarely possible to assess the legal merits of any claim without also examining the factual premise upon which that claim is advanced... As regards the word "manifestly", the Tribunal requires the Respondent's Objection to meet the test of clarity, certainty and obviousness discussed above. As regards the phrase "without legal merit", the Tribunal returns to the primary submission advanced by the Respondent at the outset of its submissions, set out above. In applying Rule 41(5), the Tribunal accepts that, as regards disputed facts relevant to the legal merits of a claimant's claim, the tribunal need not accept at face value any factual allegation which the tribunal regards as (manifestly) incredible, frivolous, vexatious or inaccurate or made in bad faith; nor need a tribunal accept a legal submission dressed up as a factual allegation. The Tribunal does not accept, however,

respondent did not satisfy the test prescribed in Rule 41(5).[36] Moreover, the tribunal established that the standard as to the satisfaction of the requirements of the said test was set high.[37] To the tribunal, the absence of legal merit in the claim needed to be "clear," "certain," "plain on its face," or "self-evident."[38]

The *Brandes v. Venezuela* tribunal reached a similar conclusion as to the high threshold that is needed for satisfaction of the requirements under Rule 41(5).[39] Brandes Investment Partners LP initiated an investment arbitration against Venezuela, alleging that the government's conduct resulted in its sale of shares in its subsidiary at a loss.[40] Pointing out the waiver and release agreement, Venezuela asserted that the said transaction was within the scope of the waiver. Ultimately, the tribunal concluded that the issues at hand were not the types of matters that could be resolved in summary proceedings as they required elaborate examination of intricate legal and factual issues.[41] Along similar lines, the *MOL Hungarian Oil* tribunal held that the full evaluation of the acquisition and operation of the investment in the respondent state and other legal arguments made within the scope of Rule 41(5) would be impossible at the preliminary stage.[42] In the tribunal's view, the respondent's Rule 41(5) objections were not "clear and certain."[43] In *PNG*

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that a tribunal should otherwise weigh the credibility or plausibility of a disputed factual allegation. Lastly, in applying Article 41 (5) to the particular case, the Tribunal accepts, of course, that it must apply these two wordings together."

36 Id. 107-117; As to the third asserted violation by the respondent, there was no need for the tribunal to assess the issue as the claimant's counsel withdrew the related third claim during the hearing; Id. 118-120.

37 Id. 88; The paragraph reads: "The Tribunal considers that these legal materials confirm that the ordinary meaning of the word requires the respondent to establish its objection clearly and obviously, with relative ease and despatch. The standard is thus set high. Given the nature of investment disputes generally, the Tribunal nonetheless recognises that this exercise may not always be simple, requiring (as in this case) successive rounds of written and oral submissions by the parties, together with questions addressed by the tribunal to those parties. The exercise may thus be complicated; but it should never be difficult."

38 Id. 83, 84, 105.

39 Brandes Investment Partners, LP v. Bolivarian Republic of Venezuela, ICSID Case No. ARB/08/3, Decision on the Respondent's Objection Under Rule 41(5) of the ICSID Arbitration Rules, 2 February 2009.

40 Id. 15.

41 Id. 71-72.

42 MOL Hungarian Oil and Gas Company Plc v Republic of Croatia, ICSID Case No. ARB/13/32, Decision on Respondent's Application under ICSID Arbitration Rule 41(5) of the ICSID Arbitration Rules, 2 December 2014, ¶ 46.

43 Id.

v. Papua New Guinea, the tribunal highlighted the time-related limitations of the preliminary examination proceeded from the invocation of Rule 41(5).[44] The tribunal pointed out the inappropriateness of discussing novel issues of law in a summary fashion, "which would inevitably limit the Parties' opportunity to be heard and the Tribunal's opportunity to reflect."[45] Moreover, the tribunal made it clear that "Rule 41(5) is not intended to resolve novel, difficult or disputed legal issues, but instead only to apply undisputed or genuinely indisputable rules of law to uncontested facts."[46]

The above-mentioned tribunals' determinations of a very high threshold in terms of characterizing claims as manifestly meritless and accordingly their denial of Rule 41(5) objections of the respondents have contributed to the emergence of severe criticism of the said rule. While some commentators contend that Rule 41(5) is just another layer of procedure that drives up the costs and causes delay, others considered the said rule inadequate as a screening tool aimed at thwarting frivolous claims.[47] Similarly, some commentators expressed their concerns about the possibility of the rule being abused by respondents to delay the proceedings and to add more financial burden on claimants.[48]

However, the subsequent cases in which Rule 41(5) invoked evinced that the initial criticisms were not entirely justified. *Globex v. Ukraine* is one of these cases the outcome of which was an indicator of the fact that Rule 41(5) was an efficient tool to weed out unmeritorious claims.[49] Global Trading Resource Corp. and Globex International Inc. brought an investment arbitration claim against Ukraine due to alleged violation of a contractual agreement. Ukraine submitted a preliminary objection invoking Rule 41(5) and asserted that the transactions in question were exclusively commercial and therefore could not be considered as an "investment" within the meaning of Article 21(5) of the ICSID Convention.[50] The tribunal found for the respondent and concluded that "the sale and purchase contracts entered into by the Claimants are pure commercial transactions that cannot on any

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[44] PNG Sustainable Development Program Ltd. v. Independent State of Papua New Guinea, ICSID Case No. ARB/13/33, Decision on Respondent's Application under ICSID Arbitration Rule 41(5) of the ICSID Arbitration Rules, 28 October 2014, ¶ 94.

[45] Id.

[46] Id. 89.

[47] Lars Markert, Improving Efficiency in Investment Arbitration, 4 Contemp. Asia Arb. J. 215 (2011), at 232.

[48] Id.

[49] Global Trading, supra note 22.

[50] Id. 41.

interpretation be considered to constitute 'investments' within the meaning of Article 25 of the ICSID Convention."[51] Accordingly, Globex's claims were found manifestly without legal merit under Rule 41(5).[52]

The tribunal in the *RSM v. Grenada* reached a similar conclusion.[53] Upon losing an ICSID case against Grenada, which involved a contractual dispute regarding a petroleum exploration, RSM and others brought a second claim before ICSID for the same dispute. Objecting to the claims under Rule 41(5), Grenada asserted that the claimant's attempt to reopen the procedures of a dispute that was previously decided constituted "a clear abuse of process."[54] The respondent also contended that the claim needed to be dismissed under the collateral estoppel doctrine.[55] Dismissing the claims, the tribunal held that it cannot revisit the conclusion of the prior tribunal and that "each of the Claimant's claims is manifestly without legal merit."[56]

The very reason for the adoption of Rule 41(5) was the need to create a tool to counter investor's abuse of the ISDS regime by way of bringing meritless claims to impose burdens over host states in order to gain leverage. Although the early awards involving the invocation of the said rule sparked criticisms in terms of its efficiency, subsequent cases proved that it could be successfully employed as a deterrent against frivolous claims. Arbitral case law, however, points out that the convenience brought by the said rule is offset by a very high threshold that a respondent state should surmount to be able to obtain an early dismissal award. Indeed, for this rule to work, claimants' claims must be clearly unmeritorious or explicitly abusive. As can also be seen from arbitral case law, in addition to objections on merits, respondent states could also raise jurisdictional objections under Rule 41(5).[57]

States' growing grievances in respect of frivolous claims galvanized other arbitration institutions into action as well. In 2016, a new mechanism was introduced by the Investment Arbitration Rules of the Singapore International Arbitration Center (SIAC Investment Rules)

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[51] Id. 57.

[52] Id. 58.

[53] Rachel S. Grynberg, Stephen M. Grynberg, Miriam Z. Grynberg & RSM Production Corp. v. Grenada, ICSID Case No. ARB/10/6, Award, 10 December 2010.

[54] Id. 4.6.15.

[55] Id. 4.6.4.

[56] Id. 4.6.4.

[57] Brandes, supra note 39, ¶ 50.

aiming at dismissing unmeritorious claims and defenses.[58] Rule 26 of the SIAC Investment Rules prescribes three situations in which parties can request the early dismissal of a claim or defense: the claim or defense is manifestly without legal merit, manifestly outside of the tribunal's jurisdiction or manifestly inadmissible.[59]

Unlike Rule 41(5) of ICSID Arbitration Rules, Rule 26 of the SIAC Investment Rules concerns not only investors' claims but also defenses of host states. It also adds two more grounds for early dismissal, which are lack of jurisdiction and admissibility. This expansion of the scope of the early dismissal mechanism created by ICSID painted a promising picture with respect to curtailing frivolous claims.

In addition to the above-mentioned institutional responses to unmeritorious claims, investment treaties started to incorporate clauses aiming at early dismissal of frivolous or abusive claims. CAFTA-DR is one of the treaties that contain such a clause.[60] According to the Article 10.20.4 of CAFTA-DR "a tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favor of the claimant may be made."[61] The article prescribes that tribunals need to consider the likelihood of success of the claim when faced with a preliminary objection aiming at the early disposition of the claim.[62] Different from ICSID's Rule 41(5), Article 10.20.4 of CAFTA-DR does not necessitate the claim to be "manifestly without legal merit." It advises tribunals to evaluate whether a favorable award may be made in the claimant's favor. The *Pac Rim* tribunal touched upon the matter:

"The Tribunal does not consider that the standard of review under Article 10.20.4 is limited to 'frivolous' claims or 'legally impossible' claims, contrary to the submissions of the Claimant. These words could have been used by the Contracting Parties in agreeing CAFTA; but all are significantly absent. Moreover, the implied addition of these or similar

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[58] 2017 Investment Arbitration Rules of the Singapore International Arbitration Center, available at: https://www.siac.org.sg/our-rules/rules/siac-investment-arbitration-rules , (last accessed 18 January 2022). The SIAC Investment Rules became operational on 1 January 2017.

[59] Id. Article 26(1).

[60] The Dominican Republic– Central America Free Trade Agreement (CAFTA-DR) is in force since 1 July 2006. The United States, The Dominican Republic, El Salvador, Costa Rica, Honduras, Guatemala, and Nicaragua are the current parties.

[61] CAFTA-DR, Article 10.20.4

[62] Ksenia Polonskaya, Frivolous Claims in the International Investment Regime: How CETA Expands the Range of Frivolous Claims That May Be Curtailed in an Expedient Fashion, 17 Asper Rev. Int'l Bus. & Trade L. 1 (2017), at 24.

words would significantly restrict the arbitral remedy under Article 10.20.4, when the structure of this provision permits a more natural and effective interpretation consistent with its object and purpose."[63]

CETA[64] also contains mechanisms to counter unmeritorious claims. Interestingly, CETA separately accommodates the mechanisms prescribed in Rule 41(5) of the ICSID Arbitration Rules and the Article 10.20.4 of CAFTA-DR. While Article 8.32 enables the respondent state to file an objection for the claims that are "manifestly without legal merit,"[65] Article 8.33 under the title "claims unfounded as a matter of law" capacitates the respondent to submit a preliminary objection if the submitted claim is not "a claim for which an award in favor of the claimant may be made."[66] Article 9.23(4) of the Comprehensive and Progressive Agreement for Trans-Pacific Partnership (hereinafter CPTPP) also adopts almost the same language in Articles 8.32 and 8.33 of CETA.[67] These agreements do not contain any explicatory text to be employed to distinguish the claims manifestly without legal merit from the ones that may not lead to a favorable award for the claimant. While proving a claim's legally meritless nature necessitates respondent states to surmount a very high threshold, asserting the low likelihood of success of a claim imposes much less burden on them. Incorporation of these two mechanisms into treaties is a clear indication of the drafters' intention to address frivolous claims expeditiously and efficiently.

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[63] Pac Rim Cayman LLC v. The Republic of El Salvador, ICSID Case No. ARB/09/12, Decision on The Respondent's Preliminary Objections Under CAFTA Articles 10.20.4 and 10.20.5, 2 August 2010, 108.

[64] The Comprehensive Economic and Trade Agreement between the European Union and Canada (CETA) provisionally entered into force on 21 September 2017. The approvals of the national parliaments of the member countries of the European Union are needed for CETA to take full effect. Details are available at: https://ec.europa.eu/trade/policy/in-focus/ceta/ (last accessed 19 December 2021).

[65] Article 8.32 of CETA reads: "The respondent may, no later than 30 days after the constitution of the division of the Tribunal, and in any event before its first session, file an objection that a claim is manifestly without legal merit."

[66] Article 8.33 of CETA reads: "Without prejudice to a Tribunal's authority to address other objections as a preliminary question or to a respondent's right to raise any such objections at an appropriate time, the Tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim, or any part thereof, submitted pursuant to Article 8.23 is not a claim for which an award in favour of the claimant may be made under this Section, even if the facts alleged were assumed to be true."

[67] Comprehensive and Progressive Agreement for Trans-Pacific Partnership (CPTPP) is effective since 30 December 2018. Article 9.23(4) of CPTPP reads: "a tribunal shall address and decide as a preliminary question any objection by the respondent that, as a matter of law, a claim submitted is not a claim for which an award in favour of the claimant may be made under Article 9.29 (Awards) or that a claim is manifestly without legal merit."

Incorporation of early dismissal clauses into institutional rules and investment treaties as a deterrent mechanism to curtail frivolous claims has contributed to the efforts to enhance the efficiency of the investor-state dispute settlement system. Nevertheless, the structural defects of the ISDS system together with its pro-investor bias deprive the arbitrators of employing such mechanisms efficiently. Inconsistency of arbitral awards is one of the central structural defects of the system. Investor-state arbitration has allowed no room for *stare decisis*, which appears to be the most promising cure for inconsistency. This is one of the main consequences of the absence of hierarchy among arbitral tribunals.[68] The absence of *stare decisis* conduces toward divergent interpretations of frivolous claims by arbitrators. An arbitrator's understanding of a claim that is manifestly without legal merit could be quite different from that of his colleagues. Similarly, the way an arbitrator evaluates the likelihood of success of a claim may differ considerably from a different arbitrator's perception of the matter. Consequently, the prevalence of unjustified inconsistency of the decisions involving frivolous claims impairs the effective application of early dismissal mechanisms prescribed by investment treaties and rules of arbitral institutions.

The inconsistency problem in investor-state arbitration is a deep-seated one, the remedy of which resides in putting radical reforms of ISDS into practice. To address this problem, on a multilateral basis, various reform options proposed within the context of UNCITRAL's work in ISDS reform including, but not limited to, creating a permanent international investment court with full-time sitting judges, introducing appellate review mechanisms and offering guidance to arbitral tribunals.[69]

The remuneration system of arbitrators is another structural defect negatively affecting the early curtailment of frivolous claims. In general, an arbitrator's compensation in investor-state arbitrations is commensurate with the time she spends on the proceedings. In other words, an arbitrator's financial gains hinge upon the continuity of the dispute she was referred to. To illustrate, members of an ICSID tribunal, in addition to the reimbursement of the travel-related expenses, can

[68] SGS Societe Generale de Surveillance S.A. v. Pakistan, ICSID Case No. ARB/01/13, Decision of the Tribunal on Objections to Jurisdiction, 6 August 2003, ¶ 97.

[69] UNCITRAL Working Group III Working Paper, (Document no: A/CN.9/WG.III /WP.150), 28 August 2018, at 14-17.

earn USD 3,000 in a day for her work in respect to the proceedings.[70] That being the case, one may argue that it would not be puzzling to observe an inclination among arbitrators towards allowing frivolous claims to proceed.

Making adjustments in the remuneration system of the arbitrators would provide only an insignificant amount of contribution to the efforts aiming at addressing the problem. This is mainly due to the fact that the root cause of the negative effect of the remuneration system of arbitrators over addressing frivolous claims is the broad discretion of arbitrators primarily originating from the absence of *stare decisis* in the ISDS system as discussed above. In this respect, this author suggests that a code of conduct for members of ISDS tribunals containing provisions that prescribe measures against arbitrators whose conduct is proven to be shaped by financial motives needs to be developed. Indeed, the development of such a code has been one of the discussion points within the ongoing ISDS reform process under the auspices of UNCITRAL.[71]

B. SECURITY FOR COSTS

As an interim measure, security for costs serves the purpose of providing financial guarantee to cover adverse costs orders.[72] As one of the hot topics remaining on the ISDS agenda, security for costs is primarily regarded as a mechanism to curtail frivolous claims. Defending an ISDS claim is rather expensive. The average amount a state spends in defending itself against an ISDS claim is USD 5 million.[73] Naturally, this amount makes states be enthusiastic about employing practical tools that would help curtailing initiation of unmeritorious claims by foreign investors. In certain instances, investors may want to disingenuously pursue a claim that lacks legal merit to secure a settlement value. To avoid such a scenario that may lead to spending

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[70] ICSID Cost of Proceedings, ICSID Website, available at: https://icsid.worldbank.org/en/Pages/services/Cost-of-Proceedings.aspx (last accessed 19 December 2021)

[71] UNCITRAL, Report of Working Group III (Investor-State Dispute Settlement Reform) on the work of its thirty-eighth session (Vienna, 14–18 October 2019), (Document no: A/CN.9/1004), 23 October 2019, available at: https://undocs.org/en/A/CN.9/1004, (last accessed 17 January 2022).

[72] Kirstin Dodge, Jonathan Barnett, Lucas Macedo, Patryk Kulig, Third-Party Funding and Reform of the ICSID Arbitration Rules, REVISTA ROMÂNĂ DE ARBITRAJ 3/2021, at 24. Available at:

https://nivalion.com/uploads/pdf/Romanian_Arbitration_Journal_no_3_2021_Excerpt.pdf (last accessed 10 February 2022)

[73] See supra note 23.

taxpayer funds to counter baseless claims, states would want to request security for costs. It would not be irrational to contend that a claimant would not be willing to deposit the estimated costs of the respondent upfront for a claim that would ultimately fail due to weak legal merit.

Security for costs came into the picture mainly to address investors' non-compliance with cost awards in favor of respondent states.[74] According to a survey conducted by the ICSID Secretariat, claimants did not comply with 12 out of 34 awards related to costs or damages.[75] The high frequency of investors' non-compliance provoked states to take action that has been manifesting itself in the form of modifications in international instruments regulating investment arbitration. Investment treaties and arbitration rules are increasingly including security for costs provisions requiring parties to deposit the estimated cost of the other party in early proceedings to be used as a security from which the party that would obtain a favorable cost award can recover its expenses later on.[76] ICSID also considered this trend in its modernization process and included security for cost provisions in the proposals for amendment of its arbitration and additional facility rules.[77]

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74 Martina Polasek & Celeste E. Salinas Quero, 'Chapter 21: Security for Costs: Overview of ICSID Case Law', in Sherlin Tung , Fabricio Fortese , et al. (eds), Finances in International Arbitration: Liber Amicorum Patricia Shaughnessy, (© Kluwer Law International; Kluwer Law International 2019) pp. 387 – 417, at 387.

75 See https://icsid.worldbank.org/en/Documents/about/Report%20on%20ICS ID%20 Survey.pdf (last accessed 31 December 2021); See also Stavros Brekoulakis & Catherine Rogers, 'Third-Party Financing in ISDS: A Framework for Understanding Practice and Policy', Academic Forum on ISDS Concept Paper 2019/11, 31 July 2019, at 23.

76 E.g., Agreement between the Government of the Republic of India and the Government of the Republic of Belarus for the Promotion and Protection of Investments, Article 28, available at https://investmentpolicy.unctad.org/international-investment- agreements/treaty-files/5724/download (last accessed 4 April 2020); The Slovakia-Iran BIT (2016), Article 2; The New EU-Mexico Agreement-The Agreement in Principle, Articles 22 and 30 (2018); European Union-Viet Nam Investment Protection Agreement (signed on 30 June 2019), Article 3.48, available at https://trade.ec.europa.eu/doclib/press/index.cfm?id=1437, (last accessed 4 December 2021); The Australia-Indonesia FTA (2019), Article 14.28; The Arbitration Rules of the Hong Kong International Arbitration Centre (HKIAC) (2013), Article 24; The Arbitration Rules of the London Court of International Arbitration (LCIA), (2014), Article 25.2; The Investment Arbitration Rules of the Singapore International Arbitration Centre (SIAC), (2017), Article 24(j); The Rules of the Vienna International Arbitral Centre (VIAC), (2018), Article 33(6); The Arbitration Rules of the Arbitration Institute of the Stockholm Chamber of Commerce (SCC), (2017), Article 38.

77 Proposals for amendment of the ICSID Rules, Working Paper 3, Volume 1, August 2019, available at:

https://icsid.worldbank.org/en/Documents/WP_3_VOLUME_1_ENGLISH.pdf, (last accessed on 19 December 2021). In this document, security for costs regulated in the Rule 52 of the Arbitration Rules and in Rule 62 of the Additional Facility Rules.

Since the current ICSID rules do not contain any provisions explicitly regulating security for costs, applicants in ICSID arbitrations have invoked provisions regulating tribunals' inherent powers or provisional measures instead.[78] Similarly, UNCITRAL Arbitration Rules vest the tribunals with the authority to issue interim measures awards, which has been an avenue for respondent states when demanding security for costs.[79]

Addressing security for costs requests could be quite challenging for tribunals as it warrants striking a balance between an impecunious party's right to access to justice and the other party's right to collect on a possible favorable costs award. This task is rather demanding in particular when the application for security for costs is made in relation to investor misconduct. In *EuroGas v. Slovak Republic,* the tribunal highlighted the exigence of exceptional circumstances to grant security for costs.[80] In the tribunal's view, the circumstances "where abuse or serious misconduct has been evidenced" are regarded as exceptional, and it was not the case in the proceedings before it.[81] Similarly, the tribunal in *South American Silver Limited v. Bolivia* rejected Bolivia's request for security for costs due to the lack of extreme and exceptional circumstances.[82] The tribunal noted:

"In relation to the necessity and the urgency of the measure, investment arbitration tribunals considering requests for security for costs have emphasized that they may only exercise this power where there are extreme and exceptional circumstances that prove a high real economic risk for the respondent and/or that there is bad faith on the part from whom the security for costs is requested."[83]

As with ICSID's early dismissal mechanism, arbitral tribunals have set a high threshold to grant security for costs awards. Impecuniosity of

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78 Polasek, supra note 74, at 388.

79 Article 26 of the UNCITRAL Arbitration Rules sets out the rules governing interim measures at great length.

80 EuroGas Inc. and Belmont Resources Inc. v. Slovak Republic, ICSID Case No. ARB/14/14, Procedural Order No. 3, 23 June 2015, 121.

81 Id. 123; See also Commerce Group Corp. and San Sebastian Gold Mines, Inc. v. Republic of El Salvador ICSID Case. No. ARB/09/17, Annulment Proceeding, Decision on El Salvador's Application for Security for Costs, 20 September 2012, ¶ 45.

82 South American Silver Limited v. Bolivia, PCA Case No. 2013-15, Procedural Order No.10, 11 January 2016, 59.

83 Id. The tribunal further elaborated: "[i]n sum, the general position of investment tribunals in cases deciding on security for costs is that the lack of assets, the impossibility to show available economic resources, or the existence of economic risk or difficulties that affect the finances of a company are not per se reasons or justifications sufficient to warrant security for costs."

the claimant or third-party funders' involvement have not sufficed by themselves for the threshold.[84] Likewise, the frivolousness of a claim has needed to be evidenced, which could be quite compelling, particularly in early proceedings.[85] As the tribunal in *Lighthouse v. Timor-Leste* observed: "Something more is required."[86] Relatedly, ICSID case law demonstrates that, between 1984 and 2019, out of 43 cases in which security for costs were requested, only in two of them was it granted.[87] The high threshold set by tribunals and the absence of specific provisions regulating security for costs in ICSID rules seem to be the main reasons behind this low number. This ratio has a comforting effect over an investor as to bringing frivolous claims. She is well aware that the claim would likely fail, and therefore, there is no point in making an upfront payment for security for a claim that lacks legal merit. Still, one has to bear in mind that, bringing an investment arbitration claim, by itself, even if it lacks legal merit, provides the investor with a considerable bargaining power against the respondent state in the course of arbitral proceedings.

In present-day conditions, largely due to the absence of regulation, it is hard to see security for costs as a practical tool to curtail frivolous claims. Nevertheless, increasing inclusion of security for costs provisions in investment treaties and institutional arbitration rules bespeaks the positive trend towards more effective employment of this mechanism. Thus, in lieu of invoking provisions on provisional measures that require high legal standards, respondent states will be able to request from tribunals the application of the security for cost provisions. Drafting these provisions in a way that provides flexible requirements and a relatively low threshold for legal standards would help tribunals to grant security for costs more comfortably.[88] An investor who feels the pressure of having to pay security for costs upfront would hesitate to

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[84] EuroGas, supra note 78, 122,123.; RSM Production Corporation v. Saint Lucia, ICSID Case No. ARB/12/10, Decision on St. Lucia's Request for Security for Costs, 13 August 2014, 75-82.

[85] EuroGas, supra note 78, 121.

[86] Lighthouse Corporation Pty Ltd and Lighthouse Corporation Ltd, IBC v. Democratic Republic of Timor-Leste ICSID Case No. ARB/15/2, Procedural Order No. 2, Decision on Respondent's Application for Provisional Measures, 13 February 2016, 61.

[87] These cases are: RSM (supra note 53) and Luis García Armas v. Bolivarian Republic of Venezuela, ICSID Case No. ARB(AF)/16/1, Procedural Order No. 8 concerning provisional measures, 20 June 2018. (The latter was consolidated with Manuel García Armas et al. V. Bolivarian Republic of Venezuela, PCA Case No. 2016-08, Procedural Order No. 9, 20 June 2018); See also Polasek, supra note 74, at 403.

[88] Academic Forum on ISDS, Working Group I, Paper on: Excessive Costs & Insufficient Recoverability of Cost Awards, 14 March 2019. Available at: https://www.cids.ch/images/Documents/Academic-Forum/1_Costs_-_WG1.pdf (last accessed 1 January 2022)

bring frivolous claims as the chances of him getting his money back would be slim. Some of the new generation investment treaties contain expressions like "reasonable doubt,"[89] "reasonable grounds,"[90] or "a reason to believe,"[91] which provides arbitral tribunals with plenty of room for interpretation when assessing the security for costs requests. Admittedly, the high number of investor non-compliance with adverse cost awards necessitates adopting such flexible language that would help tribunals in providing a positive contribution to reliability and prestige of investor-state arbitration through granting security for costs. Therefore, it becomes more of an issue for the investment arbitration community, in particular direct stakeholders of UNCITRAL's ISDS reform process, to endeavor to achieve widespread employment of the security for costs mechanism.

C. THIRD-PARTY FUNDING AND FRIVOLOUS CLAIMS

The effects of third-party funding practice over frivolous ISDS claims has been a contentious issue. Some commentators suggest that a third-party funder plays a filtering role when it examines the case, which helps getting rid of most of the frivolous cases because the funder does not want to lose its investment.[92] On the other hand, others suggest that through enabling investors to bring claims without having to allocate funds for legal representation in the case and risk diversification by way of portfolio funding, third-party funding actually causes a rise in the number of said cases.[93]

The lack of a consensus over the definition of frivolous claims in the context of ISDS makes it rather challenging to determine the effects of third-party funding on these claims. Identification of frivolous claims is compelling due to various reasons. For instance, receiving remuneration per case or hour might incentivize an arbitrator to allow a frivolous case to proceed.[94] In a similar vein, arbitrators in an ISDS setting do not necessarily have to interpret the language of investment treaties the same way the state parties do. Put differently, there may occur a gap between the state parties' interpretation of a treaty provision

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89 E.g., Slovakia-Iran BIT (2016)

90 E.g., EU-Vietnam FTA (2019)

91 E.g., India-Belarus BIT (2018)

92 Guven, supra note 5, at 21.

93 Id.

94 M. Üzeyir Karabıyık, Remedying Investor Misconduct in Investor-State Arbitration through Third Party Funding, Volume 1 Issue 2, 15-25 (2021), Indian Review of International Arbitration, at 20.

on frivolous claims and interpretation of the same text by arbitral tribunals.[95]

To those who advocate the view according to which third-party funding could play a role in preventing frivolous claims, it is mostly a matter of business.[96] To be able to make a profit, they suggest that third-party funders invest in legally sound claims that have a high likelihood of success. To figure out if the claim is worth investing in, third-party funders carry out extensive merits assessments of the claim or have a law firm do this job for them.[97] This exhaustive assessment process, they contend, enables the funders to eliminate claims that lack solid legal bases.

On the other hand, according to some commentators, third-party funding exacerbates abusive practices in arbitration litigation including frivolous claims. They suggest that if the potential recovery is large enough, a funder would be willing to take the risk even if the claim has a low probability of success due to a thin legal basis.[98] In this context, it would not be irrational to contend that this appetite of funders would incentivize an investor to claim excessive amount of compensation from the respondent state to be able to attract funders even if the case involves high risk. In a similar vein, an empirical research study looking at the cases examined by a third-party funder found that the funder preferred investing in riskier claims with a relatively lower probability of success.[99] Moreover, large corporate funders have been increasingly adopting portfolio funding, which helps them in spreading out the risks.[100] This model of funding motivates investors to bring riskier or frivolous claims, as the cost of a possible loss would be spread over the portfolio.[101] Critics of third-party funding also compare contingency fee lawyers to third-party funders to substantiate their argument that third-party funding encourages frivolous claims. While a contingency fee lawyer does have an ethical duty to advise his or her client if the claim at

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95 Guven, supra note 5, at 21.

96 Karabıyık, supra note 94, at 20.

97 ICCA-QM Report, supra note 23, Annex C, at 243.

98 Bernardo M. Cremades Román, 'Third-party Litigation Funding: Investing in Arbitration', Spain Arbitration Review | Revista del Club Español del Arbitraje, © Club Español del Arbitraje; Volume 2012 Issue 13, Wolters Kluwer España 2012, pp. 155 – 187, at 183.

99 Guven, supra note 5, at 24. (citing Daniel L. Chen, Can Markets Stimulate Rights? On the Alienability of Legal Claims (2015) 46 RAND J. of Economics 23, 25, 33)

100 ICCA-QM Report, supra note 23, at 38.

101 Frank J. Garcia, Third-Party Funding as Exploitation of the Investment Treaty System, 59 B.C. L. Rev. 2911 (2018), at 2921.

stake is frivolous, they underline that such a duty does not take place in a third-party funding agreement, which enables third-party funders to take the risk of funding frivolous claims with an expectation of unusually high returns.

The types of third-party funders need to be taken into consideration in this discussion as well. The litigation/arbitration funding market have been dominated by large investment firms providing financial services, such as hedge funds. These firms are repeat players and maintaining their reputation in the steadily expanding market is crucial for achieving their long-term financial goals. Considering this, in all likelihood, they would be hesitant about risking their reputation through contributing to abusive conduct, such as paving the way for frivolous claims. Providing portfolio funding would be preferable to them as it helps managing the risk and ensures a relatively steady profit. Then again, medium or small-sized new entrant companies in the third-party funding market may be more enthusiastic about engaging in risky and frivolous claims that might yield exceptionally high returns that would help them take root in the market and establish a reputation.[102] It would be fair to expect an augmentation in the number of new entrant companies as the third-party funding market is continuously expanding. This surge would make the competition among the funders even fiercer, which could create an atmosphere in which even unmeritorious claims would be in high demand.

The lack of empirical evidence regarding whether third-party funding drives up the number of frivolous cases in ISDS makes producing a comprehensive analysis exceptionally difficult.[103] It is partly due to the fact that third-party funding is an unregulated area of practice. The need for regulating third-party funding in investment arbitration was brought before the UNCITRAL's Working Group III within the ambit of the ISDS reform process. The continuous expansion of third-party funding would produce more data on the effects of the practice over ISDS. Along with prospective regulation of the practice through ISDS reform, this data would help produce a comprehensive analysis of how third-party funding affects frivolous cases.

[102] Karabıyık, supra note 94, at 22.

[103] ICCA-QM Report, supra note 23, at 204.

CONCLUSION

The structural deficiencies of the ISDS system and their associated repercussions, in particular on investors' behaviors in arbitration proceedings, have been a growing concern. Host states have started raising their voices against abusive practices of foreign investors that rely on the deficiencies of the system. This reaction begat the ISDS reform, a process that has been conducted on different levels and platforms. Frivolous claims have come to the fore as one of the most employed abusive tactics by investors. An ISDS claim, even if it lacks legal merit, lays burden on the host state mostly in the form of regulatory chill, reputational harm, and undue durations and costs.

This article analyzes the tools and mechanisms that can be employed to counter frivolous claims. Early dismissal mechanisms incorporated in the rules of arbitral institutions is one of them. Although it may seem that these mechanisms provide a convenient solution to states for dismissing unmeritorious cases, arbitral case law demonstrates that states need to surmount a very high threshold to get the claim dismissed at the initial phase of the proceedings. This article suggests that incorporating detailed articles on early dismissal of frivolous claims into international investment agreements to lower the high threshold set by arbitral tribunals, would be helpful. However, even with such measures, the structural defects of the ISDS system can prevent effective employment of early dismissal mechanisms by arbitrators. Security for costs is another tool that was developed to curtail frivolous claims in ISDS proceedings. Nevertheless, as was the case for early dismissal mechanisms, tribunals have adopted a high threshold to grant security for costs awards. This article suggests use of flexible language in provisions on security for costs in investment treaties and rules of arbitral institutions to provide arbitrators with ample room for interpretation when assessing the relevant requests. The effect of third-party funding on frivolous claims is also discussed in this article. Third-party funding is a relatively new phenomenon that induces conflicting views. While certain scholars contend that third-party funding curtails frivolous claims due to the fact that funders prefer to fund claims with strong legal bases, others are of the view that third-party funders may prefer to take the risk and fund a frivolous claim if the potential return is high enough. In reality, the lack of sufficient data on third-party funding and the unregulated nature of the said practice make it rather challenging to determine whether it helps in curtailing frivolous claims.

All the three tools analyzed in this article have been discussed in one way or another in the ISDS reform process. This process, in particular the one that is conducted by UNCITRAL, has mostly focused on procedural issues. Nevertheless, frivolous claims and the tools to

address them concern not only procedural but also substantive features of ISDS. Indeed, separating procedural issues from substantive ones in ISDS reform is not convenient as they are intricately related. Therefore, a holistic approach involving both procedural and substantive matters is needed in the ISDS reform process to be able to effectively cope with frivolous claims as well as other types of abusive conduct.

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