



Carolina Ramirez
Managing Director
VANNIN CAPITAL



LATIN AMERICA AND THIRD PARTY FUNDING: > A GROWING PHENOMENON

The past few years has seen a significant increase in the use of third party funding in the US and this shows no sign of slowing down. What has also become evident, is that the growth of third party funding is in fact a global phenomenon, reaching previously untapped markets such as Asia, the Middle East and Latin America. As one of Vannin's most recent hires in New York I have witnessed the potential for third party funding in Latin America first-hand. Many of the cases that have come across my desk have had a Latin American component to them, whether they have originated in the region or simply involved Latin American companies or Multinationals operating or doing business in Latin America. This article highlights third party funding in Brazil, as it is arguably the region's largest market and has seen a major uptick in third party funding in recent years.

Why Brazil?

Third party funding is a recent phenomenon in the Brazilian legal market, with practitioners estimating its arrival onto the Brazilian legal scene as recently as two years ago. Compared with other Latin American markets, Brazilian practitioners are highly attuned to the existence of third party funding and have embraced it as a potential tool in settling disputes. This growth has in part, been attributed to the liquidity crisis that has followed the economic recession that has plagued Brazil in recent years, as well as the fall-out in the aftermath of Operation Car Wash or Operação Lava Jato and the increased use of arbitration.

Perception of third party funding

Despite the increasing use of third party funding in Brazil, there remains a general perception that it is used predominately by companies facing liquidity constraints. This notion is changing, however, and "although many doubts still surround third party funding in Brazil (due to the lack of specific regulation and the market's relative inexperience with third party funding) the overall sentiment in Brazil is that third party funding is beneficial for the dispute resolution system in the country as a whole."⁸ Moreover, "general concern with respect to the nature and involvement of the funder's role seems to have been overcome and third party funding is now perceived as desirable rather than risky financing arrangement."⁹ However, as one practitioner astutely points out, "case law on the matter is scarce and major Brazilian arbitration chambers do not publish their precedents, so parties (be it funders, funded parties or adversaries to a funded party) still have to deal with a reasonable (and potentially damaging) degree of uncertainty."¹⁰ Still, various practitioners already recognise the numerous benefits of third party funding such as minimising litigation risks, freeing up capital for companies to continue their operating costs, encouraging early settlement and allowing for simplified financial statements. One practitioner forecasts that "it will evolve to [allow] major companies seeking reasonable financing that allows them to pursue their core business objectives while conducting high level litigation."¹¹

Third party funding in practice

Unlike, the US, where the cost of litigation is high, Brazilian practitioners across the board acknowledge that traditional courtroom litigation offers few, if any, benefits for third party funders. "The limited use of third party funding [in Brazil] can primarily be explained by the relatively low cost of litigation here. For instance, to file the initial statement in a judicial Lawsuit the plaintiff has to pay Court Costs of 1% of the amount in controversy (limited to a cap of BRL 75,210.00/USD 23,130.00) and to appeal, the appellant has to pay Court Costs of 4% of the amount in controversy which is also limited to a cap of BRL 75,210.00/USD 23,130.00."¹² Therefore, the low cost of filing a suit and litigation costs in general disincentivizes clients and their lawyers from seeking third party funding since costs are manageable and using third party funding "would entail forfeiting close to one-third of the potential recovery obtained in a lawsuit as a return on investment to the funder."¹³

Another obstacle facing third party funding of traditional courtroom litigation is that "court decisions are subject to several levels of appeals, meaning that cases can drag on for years before a final decision is made."¹⁴ This protracted litigation process inherently makes it more difficult for investors to predict the timing of recovery and possible judicial outcomes.



"AN INCREASING NUMBER OF INVESTMENT FUNDS THAT TRADITIONALLY FOCUSED ON THE SECONDARY MARKET BY TRADING CLAIMS (E.G. COMMERCIAL LITIGATION CLAIMS, FINANCIAL CLAIMS AGAINST DISTRESSED COMPANIES AND CLAIMS ON PUBLIC JUDICIAL BONDS -PRECATÓRIO) ARE [NOW] ALSO OFFERING THIRD PARTY FUNDING."

**GUILHERME FONTES BECHARA,
JUNIOR PARTNER
AND RAFAEL VILLAR GAGLIARDI,
DEMAREST ADVOGADOS**

By contrast, there is widespread consensus among Brazilian practitioners that arbitration is where third party funding will prove to be instrumental in enabling parties to pursue meritorious claims they may otherwise not pursue due to the prohibitive costs of arbitration in Brazil and to ultimately settling disputes.

Furthermore, "Brazil is an arbitration-friendly jurisdiction, where parties can count on a trustworthy legal system that is aligned with international standards, respects arbitration agreements and awards, and is willing to grant measures in aid of arbitration. For this reason, the largest and most notable Brazilian companies have regularly turned to arbitration to resolve their disputes, either

by including arbitration agreements in the contracts they enter into or by requiring arbitration in their by-laws. It is noteworthy that Brazil is currently the third user of the International Court of Arbitration of the International Chamber of Commerce (ICC), and that the ICC recently announced the opening of a branch in São Paulo, only its fourth office overseas. Moreover, the core changes made in the last 20 years to the legal framework of arbitration in Brazil has made this dispute resolution mechanism increasingly popular for disputes of a certain complexity and/or involving significant amounts. The downside to arbitration as opposed to litigation before state courts is the cost involved and this is where third party funding comes into play as a possible solution."¹⁵

⁸ José Antonio Fichtner, Tomaz Tavares de Lyra and Marcela Levy from ANDRADE & FICHTNER ADVOGADOS ("A&F")

⁹ Julio and Antonio from TOZZINI FREIRE ADVOGADOS

¹⁰ Id.

¹¹ Id.

¹² Antonio Celso and Erik from VELLA PUGLIESE BUOSI GUIDONI ("VPBG")

¹³ Id.

¹⁴ Guilherme and Rafael from DEMAREST ADVOGADOS

¹⁵ José Antonio Fichtner, Tomaz Tavares de Lyra and Marcela Levy from ANDRADE & FICHTNER ADVOGADOS ("A&F")

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Regulation

By and large, third party funding is unregulated in Brazil. Only recently did the Brazil-Canada Chamber of Commerce ("CAM/CCBC") – one of the most renowned institutions in Brazil – issue a resolution specifically recommending that parties disclose the use of funding at the outset of an arbitration (Administrative Resolution 18/2016).¹⁵ Practitioners predict that other arbitral institutions will soon follow suit and promulgate further regulations on the use of third party funding since there are currently no specific set of rules or guidelines governing third party funding. Given the lack of regulation of third party funding, the current climate is ripe for funders to enter the market.

The need for education

It is clear that the Brazilian legal landscape is on the precipice of major change and many anticipate that the use of arbitration, which has already become a favourite dispute resolution mechanism, will only increase in the years to come as the economy recovers from the past year's economic downturn. However, there is still a need for further education on third party funding. Clients are still relatively in the dark when it comes to the benefits of third party funding and as one practitioner points out, "stakeholders need more information about the creative financial solutions and benefits offered through third party funding. Lack of understanding of the industry [in Brazil] is still perceived as the main reason why the third party funding market in Brazil is still in its early stages."¹⁷

The future of third party funding in Brazil

Overall, practitioners are confident that there is a growing demand for third party funding in Brazil. They are highly optimistic that in the near future, once clients and practitioners have gained a certain amount of institutional knowledge, third party funding will thrive in the Brazilian legal market as it already has in more mature third party funding markets such as the US, the UK and Australia.

The resounding message is that Brazil is ripe for third party funding and that the time to enter the market is now. Furthermore, third party funding in Brazil is much better suited for arbitration than litigation. It is also clear that practitioners are enthusiastic about the prospect of having foreign third party funders with significant experience enter the market and level the playing field which has thus far been dominated by a single local Brazilian third party funder. Only time will tell, but all signs point to Brazil as potentially becoming a major player in the third party funding space.



¹⁵ Id.

¹⁶ Guilherme and Rafael from DEMAREST ADVOGADOS