

An Opportunity to Review Third Party Funding and its Recent Developments in International Arbitration

By Lena Lindinger*

With the Australian Law Reform Commission having recently published its report on third party funding in litigation, it is timely to discuss the current and evolving role of third party funding in international arbitration in Australia and globally.

Third Party Funding in International Arbitration

Third Party Funding ('TPF') arises when investors finance a legal claim in exchange for influence over case management and a financial share in the damages recoverable from the case.¹ Litigants in many European countries have been using TPF for both international commercial and investment arbitration for many years. In 2012, European funders reported a 50-50 split between court litigation and international arbitration, which included arbitration under institutions such as the International Chamber of Commerce (ICC).²

With the jurisdictions of Singapore and Hong Kong permitting third party funding in international arbitration very recently, i.e. Singapore from 10 January 2017 and Hong Kong from 1 February 2019, we want to expand upon those amendments and analyse the insights they provide as to where TPF in Australia might be heading.

Amendments in Singapore and Hong Kong

Singapore prohibited TPF in international arbitration until early 2017, when its Parliament passed the *Civil Law (Amendment) Act* (Bill No. 38/2016).³ The Act amended the law to permit third-party funding for international arbitration and related court proceedings under a number of conditions, and it also prescribed specific eligibility requirements for funders.⁴

Similarly, in Hong Kong, a code of practice on third party arbitration funding (G.N. 9048) was issued on 7 December 2018, setting out the practices and standards with which that third party funders are expected to comply. The code came into force on 1 February 2019.⁵

What is unique about these two jurisdictions permitting TPF in international arbitration is that they are the first countries to explicitly regulate TPF in international arbitration at the state level. The new laws oblige mandatory disclosure, including the identity of the funder involved. Such regulations on a national level are entirely new in the world of arbitration.⁶

¹ Maya Steinitz, *Whose Claim Is This Anyway? Third Party Litigation Funding*, 95 Minn. L. Rev. 1268, 2011.

² Maxi Scherer, *Third Party Funding in International Arbitration in Europe*, Queen Mary University of London, 2012.

³ Nicholas Turner, *Hong Kong to allow third party arbitration funding from 1 February*, Out-Law.com, 2019.

⁴ Krestin and Mulder, *Third-Party Funding In International Arbitration: To Regulate Or Not To Regulate?*, Kluwer Arbitration Blog, 2017.

⁵ Turner, above n 3.

⁶ Krestin and Mulder, above n 4.

Issues to Consider regarding Third Party Funding in Arbitration

The 2018 ICCA-QM Report on Third Party Funding identifies three principles that require close attention before entering into a funding agreement: Disclosure, Privilege and Confidentiality, and Allocation of and Security for costs.⁷ Discussion of each principle follow respectively.

Disclosure

This principle requires the funded party to reveal the facts of its funding arrangement and at the same time provide their funders with transparency. Disclosure of funding arrangements facilitates transparency and pre-emptively addresses potential conflicts of interest that may arise.

The following commentary from Ashurst highlights the increasing demand for transparency in TPF:

*'The nature of international arbitration, and in particular the mechanism for the appointment of arbitrators, raises several issues surrounding the use of third party funding. In arbitration, where the arbitrators are often selected by the parties, this gives rise to potential conflicts of interest where an arbitrator, or their colleagues or firm, have a relationship with a funder involved in the case.'*⁸ The recent developments in Singapore and Hong Kong echo the above remarks. Both regulatory frameworks deal with the issue of disclosure and provide for mandatory disclosure with respect to the identity of the funder involved.⁹

We can also reflect on the positive aspects of disclosure for a funded party: an openly funded claim demonstrates that an independent third party has faith in the merits of the claim. Moreover, disclosure in the early stages of a hearing prevents the other party from raising conflict arguments should the funded party prove successful.¹⁰

Privilege and Confidentiality

'Privilege and confidentiality' refers to the obligation to provide the funder with confidential information. This can occur as early as the preliminary stage and involves sending privileged documents and legal advice to third party funders. Whether sending these confidential documents constitutes a waiver of privilege depends on the rules of privilege in the relevant jurisdiction and should always be verified.¹¹ Some argue that 'privilege and confidentiality' is closely tied with disclosure and can therefore be attributed with similar benefits.

Allocation of Costs and Security for Costs

Views differ on the allocation of costs. Some defend the notion that TPF should not make a difference on how costs should be allocated on the outcome of the arbitration. Others argue that since the funder

⁷ *The ICCA Reports No.4 – ICCA Queen Mary Task Force Report on Third Party Funding in International Arbitration*, ICCA, 2018.

⁸ Tom Cummins et al, *Third Party Funding in International Arbitration*, Ashurst, 2018.

⁹ Horodyski and Kierska, *Third Party Funding in International Arbitration – Legal problems and Global Trends with a Focus on Disclosure Requirements*, 2017.

¹⁰ Cummins et al, above n 8.¹¹ Ibid.

¹¹ Ibid.

¹² *International Arbitration 2019: What to look out for*, Clyde & Co LLP, 2019.

exercises significant control over the claimant's behaviour in the arbitration proceedings, often directing the course of the proceedings, the adverse costs awarded have an effect on the funder.¹²

A key consideration concerning security for costs is the financial situation of the party against which the security is requested. The 2018 ICCA-QM Report on Third Party Funding suggests the following solution to eliminate the remaining concerns about the security for costs:

*An application for security costs should be determined on the basis of the applicable test, without regard to the existence of any funding arrangement.*¹³

Where Australia Fits In

Although the principles discussed above may present as challenges, they also signal potential opportunities and benefits. Given Australia's history of success in implementing regulatory regimes,¹⁴ should the government move in this direction it seems like nothing would stand in the way of a thriving TPF practice for arbitration in Australia.

Currently there is no regulation for capital adequacy of TPF in Australia. The reason behind this is the courts' highly valued separation between arbitral and litigation proceedings. Another factor according to recent observations by Ashurst, is that:

'The law exempts litigation funders from regulating managed investment schemes on the condition that the funding arrangement maintains adequate practices for managing any conflicts of interest that may arise and that those practices are documented, implemented, monitored and managed by senior management of the funder in accordance with the regulator's specifications'.¹⁵

The ALRC paper on TPF in Litigation echoes the above remarks with regards to arbitration. It recommends that regulation is required in TPF in any dispute resolution proceedings, including arbitral proceedings.¹⁷

In simple terms, third party funders in Australia currently rely on the trust that the above classified principles will be pursued. They have no legal regulations that ensure a secure arrangement between funders and funded parties. However, if Australia follows the examples of Hong Kong and Singapore, such regulations could help unify the practices nationwide, enhance the use of third party funding and subsequently encourage transparency in international arbitration.

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¹³ Tom Cummins et al, *Third Party Funding in International Arbitration*, Ashurst, 2018.

¹⁴ The Hon. Michael Ronaldson, *Fighting Australia's Over-regulation*, 2015.]

¹⁵ See *Campbells Cash and Carry Pty Ltd v Fostif Pty Limited* [2006] HCA 41; 229 ALR 58, 2006.

¹⁶ Tom Cummins et al, *Third Party Funding in International Arbitration*, Ashurst, 2018.

¹⁷ *An Inquiry into Class Action Proceedings and Third Party Litigation Funders*, Australian Law Reform Commission, 2019.