Kluwer Arbitration Blog

Third-party funding and arbitration law-making: the race for regulation in the Asia-Pacific

Kabir Singh, Sam Luttrell and Elan Krishna (Clifford Chance Asia (in formal law alliance in Singapore between Clifford Chance Pte Ltd and Cavenagh Law LLP)) · Thursday, July 14th, 2016

In recent years, international arbitration has emerged as a high-growth area for the litigation funding industry. All the major funders now have international arbitration cases in their portfolios, and many are aggressively seeking more – especially investment treaty cases. But the participation of funders in international arbitration raises a number of issues, some national and legal, and others international and ethical. As the number of funded users of international arbitration increases, regulation of third-party funding ("**TPF**") is becoming an important factor in choosing the seat, and awareness of this is driving legislative change in this area.

The law of the seat usually serves two main functions: first, it provides basic rules for the conduct of the arbitration (most of which are subject to party autonomy); second, it governs the relationship between the arbitral tribunal and the local courts (including judicial review and enforcement of the award).

But there is more to the *lex arbitri* than the arbitration act. The law of the seat also supplies mandatory rules that, whilst not specific to arbitration, may still be applicable to the arbitral process and its participants. TPF laws are an example. If a funded party goes to arbitration at a seat where TPF is illegal then that party faces three main risks:

- If the funded party is the claimant (as is usually the case), the respondent may seek to injunct the arbitration on the basis that it is an abuse of process; alternatively, the respondent may sue the funded claimant in tort (for abuse of process or champerty and maintenance – discussed below);
- If the funded party needs the assistance of the courts of the seat, the courts may decline to assist on the basis that the funded party lacks clean hands (because it is funded);
- If the funded party prevails in the arbitration, the respondent may seek to set-aside the award on the basis that, as the product of a funded arbitration, the award is offensive to public policy.

Further, the funded party's lawyers may be at risk to the extent that they are subject to the professional conduct rules or legal practice regulations of the seat. Finally, for the funder, there is a risk that, if the funded party's assets are located in a TPF-intolerant jurisdiction, the funder may not be able to enforce its rights under the funding agreement. Experienced arbitration lawyers are aware of these risks: if they have a client that will or may need TPF, they will advise that client to choose another seat. Sophisticated legislators are aware of this and the potential it has to reduce their share of the global market for arbitration services. This is why many of the leading seats are now changing their laws to make them more TPF-tolerant. Singapore is the latest example.

Singapore prides itself on having the "Rolls Royce" of international arbitration frameworks. However, Singapore law currently prohibits TPF in both litigation and arbitration (albeit with limited exceptions):

- First, Singapore law generally treats third-party funding agreements as contrary to public policy or illegal. This policy is informed by the common law doctrines of maintenance and champerty (maintenance is the giving of assistance or encouragement to a litigant by a person who has neither an interest in the proceedings nor any other motive recognized by law as justifying interference; champerty is the maintenance of an action in exchange for share in the fruits of the proceedings).
- Second, Singapore law regards maintenance and champerty as torts at common law. An affected party could (at least in theory) sue the funded party (or parties) in tort if the affected party has suffered special damage as a result of the relevant tortious arrangement.

The Singapore Court of Appeal has stated that the principles behind the doctrine of champerty apply to all types of legal disputes and claims, including arbitration proceedings (*Otech Pakistan Pvt Ltd v Clough Engineering Ltd & Anor* [2007] 1 SLR(R) 989). There are, however, certain statutory and common law exceptions to the doctrines of maintenance and champerty. For example, the liquidator of an insolvent company is allowed to sell – to a funder or other party – a cause in action and/or the fruits of a cause of action (*Companies Act* (Cap. 50), s 272(2)(c); *Re Vanguard Energy Pte Ltd* [2015] 4 SLR 597). More generally, a third-party funding arrangement will not be struck down if (i) it is incidental to the transfer of a property right or interest; (ii) the funder has a legitimate interest in the outcome of proceedings (for example, where the funder is a beneficiary, shareholder, director, or creditor of the funded party); or (iii) there is no realistic possibility that the administration of justice will suffer as a result, taking into account the protection of the purity/due administration of justice (for example, the extent to which the funded litigant retains control over legal proceedings or has ceded such control to the funder) and the interests of vulnerable litigants, and ensuring access to justice (Re *Vanguard Energy Pte Ltd* [2015] 4 SLR 597, [43]; *Lim Lie Hoa & Anor v Ong Rebecca Jane* [1997] 1 SLR(R) 775, [46]).

On 30 June 2016, the Singapore Ministry of Law ("**MinLaw**") launched a public consultation on its proposals for enactment of a legislative framework for TPF. In particular, the proposed new legislation will (a) clarify that the common law torts of maintenance and champerty are abolished; and (b) provide that TPF contracts are not contrary to public policy or illegal in international arbitration and related proceedings.

MinLaw has also proposed a number of safeguards. For instance, MinLaw has proposed that third-party funders will only be able to enforce their rights if they satisfy a number of conditions. These include a requirement that the funder has access to funds immediately under its control sufficient to fund the relevant proceedings in Singapore. It is also proposed that lawyers will be bound to disclose the existence of a TPF agreement and the identity of the funder to a court or arbitral tribunal and every other party to the proceedings. The proposed legislation also envisages guidelines (based principally on the IBA Guidelines on Conflicts of Interest in International Arbitration) being issued in due course.

If enacted, the new legislation will reduce (even eliminate) the risk that a TPF arrangement is used as a basis for judicial intervention in the arbitration or as a premise for an application to set-aside the award (or refuse its enforcement). This will make Singapore more attractive as a seat. While TPF is often associated with smaller businesses, larger businesses increasingly use TPF products as cost/risk shifting tools. So, while the short-term market impact of these changes may be more pronounced at the "smaller end of town", in the long term it is likely that the new TPF rules will also increase Singapore's capture of cases involving larger businesses too. The changes will also mean that Singapore hosts more investor-State arbitrations from around the region, as these kinds of actions are often funded. Investor-State Dispute Settlement ("**ISDS**") is an important area for Singapore, positioned as it is in the midst of a group of countries of varying sovereign risk. Singapore is currently a party to a number of ISDS-inclusive trade and investment treaties, and a number of other major ISDS-inclusive treaties are either subject to negotiation or pending ratification. Many of these treaties offer *ad hoc* arbitration and arbitration at various regional arbitration centres, and this is where Singapore is looking to position itself with changes to its TPF rules and initiatives like the Investment Arbitration Rules proposed by the Singapore International Arbitration Centre. Finally, the changes will mean that Singapore lawyers are able to act for funded parties in international arbitrations.

In order to compete for a share of the growing volume of international arbitration cases, a seat needs to be tolerant of TPF. Indeed, comprehensive legislation is what the market wants to see. This is evident from the fact that the two leading seats in the Asia-Pacific – Hong Kong and Singapore – are almost in sync in this area. Hong Kong conducted its own legislative consultation process regarding TPF in October last year, and the Hong Kong branch of CIETAC issued draft TPF guidelines a few months ago. While TPF-intolerant seats may still be able to capture a significant volume of international commercial arbitration cases, they risk being left behind in the competition to host the growing volume of investor-State arbitrations. As these cases are often the biggest, they need to be accounted for in any legislative program designed to make a jurisdiction competitive as a seat in the years ahead.

This entry was posted on Thursday, July 14th, 2016 at 12:27 pm and is filed under Arbitral seat, Arbitration, Arbitration Act, Singapore, Third party funding
You can follow any responses to this entry through the Comments (RSS) feed. You can leave a response, or trackback from your own site.