Third-party funding: has it finally come in from the cold?

By Maria Cole

Third-party funding of the cost of dispute resolution was historically a no-go zone in both common law and certain civil law jurisdictions. However, its benefits in assisting to break down the barrier of cost in accessing civil justice saw it hailed as a saviour of the financial under-dog. It is now increasingly being given the official green light in the funding of both litigation and arbitration. What are the current international trends on third-party funding of arbitration and what is its future in New Zealand?

Third-party funding, also known as litigation funding, is where a third-party, with no legal interest in the dispute, agrees to fund some or all the costs of a party to the dispute in return for a "a slice of the action". Historically third-party funding was not permitted in New Zealand, as it breached the doctrines of "maintenance" and "champerty" and was viewed as unethical.[1] The courts saw it as against public policy over concerns it would result in conflicts of interest and encourage unmeritorious claims, and in certain countries it was a crime. In the 1960s, Lord Denning MR, the colourful former President of the Court of Appeal in England, explained the attitude:[2]

> The reason why the common law condemns champerty is because of the abuses to which it may give rise. The common law fears that the champertous maintainer might be tempted, for his own personal gain, to inflame the damages, to suppress evidence, or even to suborn witnesses. These fears may be exaggerated, but, be that so or not, the law for centuries had declared champerty to be unlawful…

Third-party funding needed an image makeover. The power and resource imbalance that often exists between potential parties to a civil dispute, together with the need to facilitate access to justice in representative and class actions, helped provide one. Over recent decades, England and Wales, and parts of Canada and the USA, have all diluted or repealed the rules around maintenance and champerty, so that "properly structured" third-party funding of litigation and arbitration is now permitted there. Australia has permitted funded class actions since the early 1990s.

Third-party funding of arbitration is a fact of life

The International Chamber of Commerce has stated that "despite reservations, the solution offered by third-party funding has now become a fact of life in the world of arbitration".

In 2017, Singapore passed a Civil Law (Amendment) Bill to permit third-party funding agreements for international arbitration. Singapore considered that third-party funding of arbitration was necessary in order to remain a competitive international arbitration hub. The Singapore Government also introduced the Civil Law (Third Party Funding) Regulations to set out eligibility requirements for third-party funders, including a requirement that third-party funders must have "paid-up share capital of not less than US$5

1 "Maintenance" is generally concerned with supporting litigation brought by others where you have no legal interest in the dispute. "Champerty" involves accepting a share of the proceeds obtained through litigation and is a particular form of maintenance. The rules around it were introduced in medieval England to prevent abuses of justice by corrupt nobles and officials lending their names to fraudulent and vexatious claims in return for a share of the profits.

2 In *Re Trepca Mines (No 2)* [1963] Ch 199.

million". Amendments were also implemented to Singapore's Legal Profession Act and Legal Profession Rules. They promote counsels' duties to their clients and require practitioners to disclose to other parties if a third-party funding agreement is in effect, along with the name of the third-party funder, on the commencement of arbitration or as early as practicable. A guidance note issued by the Council of the Law Society of Singapore on these legislative amendments can be read here[3].

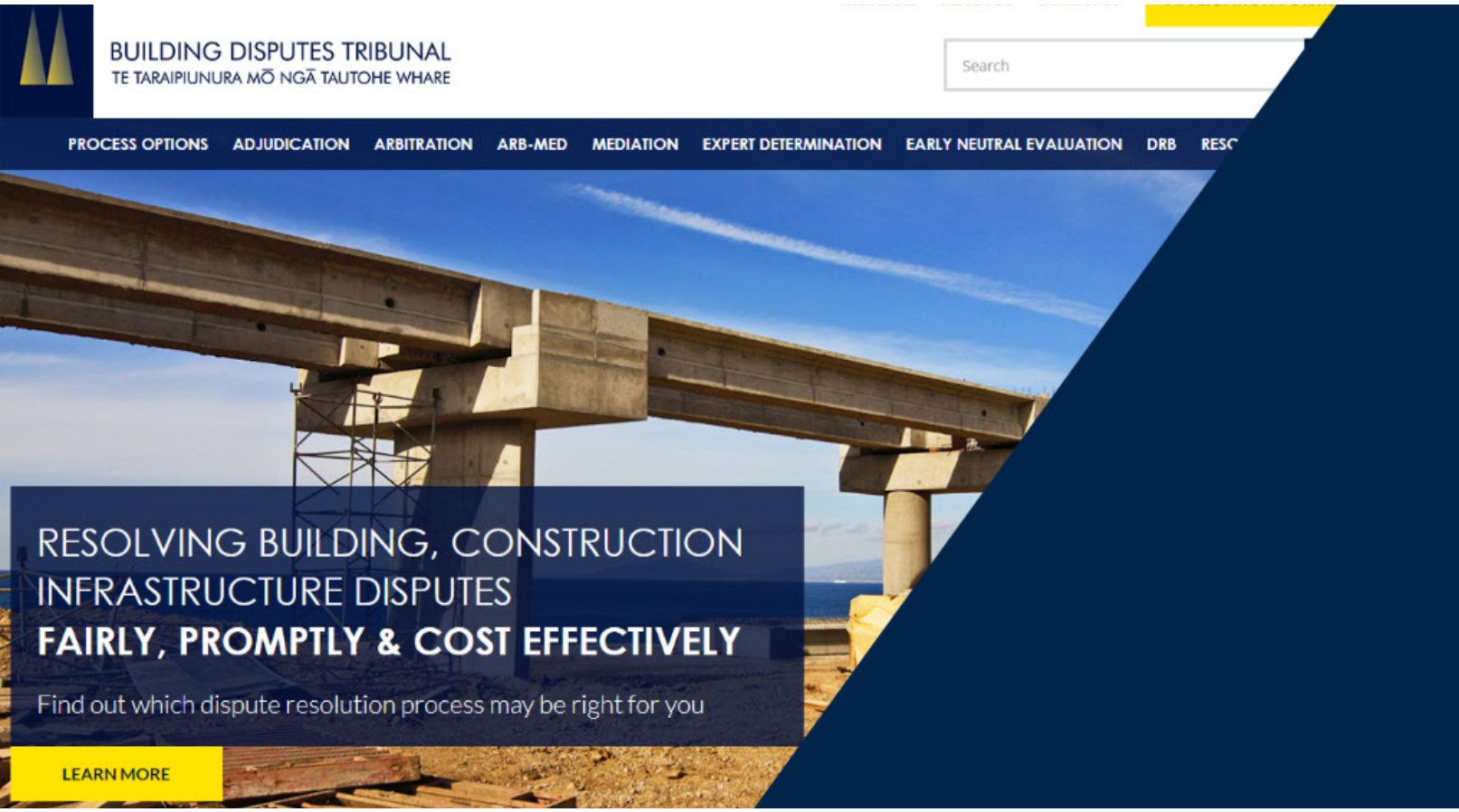
The Singapore International Arbitration Centre revised its International Arbitration Rules to permit arbitral tribunals to order disclosure of the existence of third-party funding agreements and names of third-party funders. It issued a practice note on the standards of practice and conduct of arbitrators in international arbitrators where the involvement of external funds is permissible, which can be viewed here[4].

Since third-party funding of arbitration was given the green light in Hong Kong in 2017, amendments have been enacted to the Hong Kong Arbitration Ordinance to address it directly, with the *Hong Kong Code of Practice for Third Party Funding of Arbitration* coming into force on 1 February 2019. Its purpose is to ensure that third-party funding of arbitration is not prohibited by the common law doctrines and to provide for measures and safeguards in relation to it, once again addressing issues such as capital adequacy requirements of the funder, conflicts of interest, confidentiality, and control of conduct of the arbitration. The Code of Practice and information about it which has been released by the Government of Hong Kong can be found here[5].

The rise and regulation of third-party funders

Third-party litigation funding is now an established industry and there are now, in addition to specialised third-party funding institutions, insurance companies, investment banks, hedge

3 https://www.lawsociety.org.sg/wp-content/uploads/2020/03/Third-Party-Funding-GN-10.1.1.pdf accessed on 12 February 2021.
4 http://www.siac.org.sg/images/stories/articles/rules/Third%20Party%20Funding%20Practice%20Note%2031%20March%202017.pdf accessed on 12 February 2021.
5 https://www.info.gov.hk/gia/general/201812/07/P2018120700601.htm accessed on 12 February 2021.



funds and law firms offering to finance litigation and arbitration.

Statutory and voluntary codes of conduct are being put in place to ensure the legitimacy of third-party funders and to provide best practice guidelines. In Singapore, funders must meet and continue to satisfy requirements to become "qualifying" third-party funders and if they do not do so, their rights under any funding agreement contract are not enforceable.

The Association of Litigation Funders of England & Wales, which currently has nine funder members, has a voluntary Code of Conduct for Litigation Funders (ALF[6]). It too covers capital adequacy requirements for funders and rights regarding termination and control of proceedings.

The Australian Law Commission completed an inquiry into class actions and litigation funders in 2019. It proposed a suite of recommendations to improve the regulation of litigation funders. Since August 2020, litigation funders in that country have had to hold an Australian Financial Services Licence and are required to register to conduct most class actions as managed investment schemes.

In New Zealand there is neither statutory nor voluntary regulation of funders. The Law Commission/Te Aka Matua o te Ture is currently conducting its combined review of class actions and litigation funding. In its Issues Paper, it has said that in New Zealand "the litigation funding market is relatively opaque", noting in relation to current trends:[7]

> Although claims arising out of insolvent companies continue to be an important area of activity for litigation funders, the use of litigation funding has since expanded into other contexts, including representative actions, commercial disputes and insurance claims…
>
> We have identified five domestic based litigation funders and six overseas-based funders operating in Aotearoa New Zealand. …one likely reason the market in Aotearoa

6 https://associationoflitigationfunders.com/documents/ accessed on 12 February 2021.
7 NZLC IP45, December 2020, Wellington at [14.25[, [14.34] and [14.43]. The review paper is available at https://www.lawcom.govt.nz/.

> New Zealand is still relatively small is that the lack of regulation and explicit endorsement of litigation funding by the courts means there is still some uncertainty about its legal status.

Despite this, in August 2020, global law firm DLA Piper announced[8] that it had entered into an arrangement with a publicly listed disputes financier and a litigation funder to offer access to its client, including those in the Trans-Pacific region, to GBP150m for funding large-scale litigation and arbitration. It was being offered on a financial risk-free (non-recourse) basis. The announcement says:

> *This funding offering opens up the opportunity to DLA Piper clients to pursue claims that would have otherwise been untenable due to capital constraints.*

The future of third-party funding in Aotearoa New Zealand

In 2018, Nikki Chamberlain of the University of Auckland published a study on class actions in New Zealand.[9] She states that the data reflects the rise of consumer class actions in New Zealand which, in part, have been assisted by litigation funders entering the market. Her views on the future of class actions in this country were:

> *In relation to civil procedure options for the private enforcement of class-wide wrongs, there are three main avenues to consider. First, the government could leave HCR 4.24 as it is and make no change to current procedure… Secondly, the government could promote and encourage mass alternative dispute resolution processes (i.e. class arbitration or specialist resolution services for certain types of claims) as opposed to class litigation through the High Court. Thirdly, the government could enact legislation that incorporates specific class action civil procedure rules, an action that has been taken in other jurisdictions such as Australia and the United States.*

In the recent decision of *Southern Response Earthquake Services Ltd v Ross* [2020] NZSC 126, the Supreme Court set out its view on the courts' oversight role of litigation funding in representative actions. It confirmed that the courts will continue to ensure that arrangements with litigation funders do not amount to an abuse of the courts' processes but noted:

> [86] … While the Court in *Waterhouse* said it was not the courts' role "to act as general regulators of litigation funding arrangements", the Court left open the scope of the courts' supervisory role for litigation funding arrangements in relation to representative proceedings. That said, we consider it would be premature to say there is an expectation that any litigation funding agreement should routinely be provided to the court as part of an application under r 4.24(b)…

As mentioned, the Law Commission/Te Aka Matua o te Ture is currently conducting a combined review of the law on class actions and litigation funding. The Commission has stated its *preliminary view is that litigation funding is desirable in principle and should be permitted here, as long as certain concerns can be addressed*. It lists those concerns as including funder control over litigation, the potential for conflicts of interest, funder profits, and the capital adequacy of litigation funders. It is seeking feedback by 11 March 2021 on how those concerns can be managed and whether a regulatory response is warranted.

The Law Commission lists options for the form of any regulation and oversight of litigation funding as including:

- Industry self-regulation.
- Bringing litigation funding within the scope of the Financial Markets Conduct Act 2013, as a "managed investment scheme".
- A tailored licensing system for litigation funders.
- A new statutory regime with oversight by a new statutory body.
- Court approval of funding arrangements.

Of particular interest will be how and whether issues such as a third-party funder's liability to pay security for costs, meet liability for adverse costs awards, pay a premium to obtain costs' insurance, and meeting other financial liabilities are addressed.

There is no specific mention in the Law Commission paper of third-party funding in the arbitration arena.

8 https://www.dlapiper.com/en/africa/news/2020/08/dla-piper-and-lcm-collaborate/ accessed on 16 February 2021.
9 Nikki Chamberlain, *Class Actions in New Zealand: An Empirical* Study, NZBQ Vol 24 at 132. The full article can be accessed here: Class Actions in New Zealand: an empirical study.

Summary

Third-party funding has gained international acceptance. There is enormous scope for its use in the arbitration arena in this country. Some form of oversight of the third-party funding industry in New Zealand appears inevitable and, if the industry wants to grow, desirable. The recommendations made by the Law Commission/ Te Aka Matua o te Ture will undoubtedly inform whether that oversight will be by way of the lighter touch of a voluntary regime as has been instigated in England & Wales, or a more rigorous statutory framework as implemented in Singapore. Where third-party funding of international and domestic arbitration in New Zealand sits within the current considerations remains to be seen.

About the author

Maria works as a Knowledge Manager in NZDRC's Knowledge Management Team. She was previously a civil litigation barrister for over a decade, where she gained experience in arbitration and mediation.