

Hong Kong: Law Reform Commission Recommends Allowing Third-Party Funding for Arbitration

Consultation Paper reviews Third-Party Funding in other jurisdictions, finding the practice may lead to better outcomes in disputes.

The Hong Kong Law Reform Commission published a Consultation Paper on 19 October 2015 recommending that Third-Party Funding (TPF) for arbitration taking place in Hong Kong should be permitted under Hong Kong law.

The Consultation Paper provides a comprehensive overview of the law on TPF for arbitration in Hong Kong and other jurisdictions, as well as an analysis of the potential benefits and risks of TPF in Hong Kong. The Consultation Paper can be accessed [here](#).

Third-Party Funding

TPF has been described as “the funding of claims by commercial bodies in return for a share of profits”. The practice involves a “third person” to the proceedings providing financial “assistance or support to a party to” the Proceedings.¹

A TPF arrangement for arbitration commonly provides that the Third-Party Funder will pay the Funded Party’s legal and other costs of arbitration in return for a percentage of the award or some other financial benefit from any of the financial recoveries in the arbitration. The Third-Party Funder will only be compensated from the Funded Party’s net recoveries from the proceedings (after the deduction of agreed costs and expenses).

The Consultation Paper includes a review of several jurisdictions which allow TPF. Of nine reported cases involving litigation funding in Australia, the United States and the United Kingdom, the entitlements for Third-Party Funders ranged between 8% and 55% of the proceeds of the case. In a 2014 comparative study of Third-Party Funders in *Litigation Funding*², the range of entitlements most commonly claimed by Third-Party Funders was between 20% and 45%. Further, a report published in the *Journal of International Arbitration* has suggested 15-50% as a typical range in international arbitration claims, with a median figure of around 33%.³

Arguments in Favour of TPF

Generally, TPF arrangements are motivated by a party’s lack of financial resources to pursue its own claims. However, increasingly, parties have used TPF to manage the risks of litigation or arbitration – by sharing the risk of non-recovery and the potential for recovered funds with the Third Party Funder.

Supporters of TPF argue that knowledge that a party has received TPF (and therefore can pay for and sustain the arbitration until an award is handed down) can help precipitate a compromise of the

dispute, encouraging the other side to consider settlement, potentially saving considerable time and expense for both parties.

Proponents of TPF note that, as Third-Party Funders will only fund cases which meet their investment criteria, and, in particular, cases that have a reasonable to high chance of success (with success ratings usually between 60% and 75%), TPF helps to screen out unmeritorious claims.

Status of Hong Kong Law on TPF

The question of whether the doctrines of maintenance⁴ and champerty⁵ prohibit TPF in an arbitration taking place in Hong Kong remains undecided.

TPF in litigation is permitted in Hong Kong but only in specific, limited circumstances. In *Unruh v Seeberger*⁶ Hong Kong's Court of Final Appeal upheld the validity of a TPF agreement for an arbitration conducted overseas; however, the Court expressly left open the question of whether the doctrines of maintenance and champerty apply to TPF agreements for arbitrations taking place in Hong Kong, as the issue did not arise in the case.

The Law Reform Commission's Recommendations

The Law Reform Commission unanimously concluded that reform of Hong Kong law is needed to clarify that TPF is permitted for arbitrations taking place in Hong Kong, provided that parties comply with appropriate financial and ethical safeguards.

To this end, the Law Reform Commission recommended that:

- The Arbitration Ordinance should be amended to permit TPF for arbitrations taking place in Hong Kong.
- Clear ethical and financial standards should be developed for Third-Party Funders providing TPF to parties to arbitrations taking place in Hong Kong.

The Law Reform Commission also invited submissions as to:

- Whether the development and supervision of the applicable ethical and financial standards should be conducted by:
 - a) a statutory or governmental body, whether existing or to be established, and if so, what type of body; or
 - b) a self-regulatory body, whether for a trial period or permanently and how any ethical and financial standards should be enforced
- How the applicable ethical or financial standards should address any of the following matters or any additional matters:
 - Capital adequacy
 - Conflicts of interest
 - Confidentiality and privilege
 - Extent of extra-territorial application
 - Control of the arbitration by the Third-Party Funder
 - Disclosure of TPF to the tribunal and other party/parties to the arbitration
 - Grounds for termination of TPF
 - A complaints procedure and enforcement

- Whether or not a Third-Party Funder should be directly liable for adverse costs orders in a matter it has funded
- If the answer to the above is “yes”, how such liability could be imposed as a matter of Hong Kong law, and for the purposes of recognition and enforcement under the Convention for Recognition and Enforcement of Foreign Arbitral Awards 1958
- Whether there is a need to amend the Arbitration Ordinance to provide for the Tribunal’s power to order Third-Party Funders to provide Security for Costs
- If the answer to the above is “yes”, the basis for such power as a matter of Hong Kong law, and for the purposes of recognition and enforcement under the Convention for Recognition and Enforcement of Foreign Arbitral Awards 1958

Consultation Period

The consultation period for submissions from the public will end on Monday, 18 January 2016. The possible introduction of TPF for arbitrations taking place in Hong Kong is a significant development. We encourage all parties involved or interested in arbitration to review the Consultation Paper, and comment: [Simon Powell](#) or [Ing Loong Yang](#) will be happy to forward your views and recommendations on to the Law Reform Commission.

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Endnotes

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- 1 *Uhruh v Seeberger* (2007) 10 HKCFAR 31, at para 118 (*per* Ribeiro PJ).
 - 2 Council of the Law Society of England and Wales, *Litigation Funding*, Issue 93 (2014).
 - 3 Susanna Khouri, Kate Hurford and Clive Bowman, "Third Party Funding in International Commercial and Treaty Arbitration – A Panacea or a Plague? A Discussion of the Risks and Benefits of Third Party Funding" 8(4) *Transnational Dispute Management* (2011), at 3; Eric De Brabandere and Julia Lepeltak, *Third Party Funding in International Investment Arbitration* (Working Paper No 1, Grotius Centre for International Legal Studies, 2012), at 5.
 - 4 Maintenance refers to the giving of assistance or encouragement to one of the parties to an action by a person who has neither an interest in the action nor any other motive recognized by the law as justifying his interference.
 - 5 Champerty refers to a particular kind of maintenance, namely maintenance of an action in consideration of a promise to give to the maintainer a share of the subject matter or proceeds thereof, if the action succeeds.
 - 6 (2007) 10 HKCFAR 31, at para 123 (*per* Ribeiro PJ)