

LHAG

SPECIAL ALERT

International Arbitration



Crystal Wong Wai Chin
Partner

International Arbitration

E: wwc@lh-ag.com



Lim Jia Yun Ruth
Pupil

International Arbitration

E: jylim@lh-ag.com

19 FEBRUARY 2024

Balancing Desire and Danger: Regulating Third-Party Funding in a Global Context

On 13 February 2024 (Tuesday), Minister in the Prime Minister's Department (Law and Institutional Reform) Datuk Seri Azalina Othman Said made a public statement announcing a consensus between the Malaysian Government and the European Union (EU) that regulation of third-party funding (TPF) demands heightened attention on an international scale¹. This announcement triggers timely consideration of TPF practice and regulation globally.

This e-Alert will explain the mechanism and background of TPF, set out its benefits and potential drawbacks, examine regulation of TPF in Malaysia, England and Wales, Singapore, and Hong Kong, and finally conclude that Malaysia should seek insights from other jurisdictions and tailor its own TPF regulatory measures for the benefit of Malaysians.

¹ Article in The Edge Malaysia entitled "Azalina: Malaysia, EU recognise need to regulate third-party litigation funding" on 13 Feb 2024 at 10:00PM

What is TPF?

Third-party funding (TPF) is the provision of financial support from a party not directly involved in a legal dispute (the “funder”) to one of the parties involved in the dispute (the “litigant”) for the purposes of legal proceedings. In return, the funder receives a portion of winnings or benefits resulting from the legal proceedings.

Over the past few decades, TPF has grown into a multi-billion-dollar industry in many regions, including the USA, the UK, and Australia. One example of a global litigation finance firm is Therium Capital Management Ltd, which has funded legal claims worldwide to the value of circa 100 billion USD² and is also the funder of the Sulu heirs’ claim against Malaysia.³

TPF has historical roots in the English doctrine of Champerty and Maintenance, which prohibits TPF activities and the like due to concerns of abuse in the litigation process. The threat of abuse arises from the heavy influence of the funders over the legal proceedings, driven by their primary motivation for financial gain instead of a genuine desire to amicably resolve the dispute and/or seek justice. Despite the danger of TPF being misused, countries such as Singapore and Hong Kong have legalised it for limited types of proceedings, focusing on regulating TPF activities to leverage its benefits while mitigating potential drawbacks.

² Therium’s Company Website <<https://www.therium.com/about-us/>>

³ Article in The Edge Malaysia entitled “Special Report: The Sulu heirs’ claims – A thorn in Malaysia’s side” on 25 Jul 2022 at 04:00PM

Why Is TPF Desirable Yet Dangerous?

Benefits	Drawbacks
<p>TPF increases access to justice for those unable to afford litigation fees, who do not meet the criteria for legal aid.</p>	<p>TPF parties may potentially abuse the justice process, being tempted to “inflare damages, suppress evidence, or suborn witnesses”⁴ for the sake of winning litigation, disregarding fairness or justice.</p>
<p>TPF could be vital for group litigation, comprising a high number of claimants who individually suffered small losses, making claims uncommercial otherwise.</p>	<p>TPF parties may compromise on ethical standards, driven purely by financial interests.</p>
<p>TPF is crucial for pursuing justice in meritorious claims, enabling cases that might otherwise go unexplored due to prohibitive costs.</p>	<p>Lack of transparency in funding arrangements may undermine the integrity of the justice system and raise concerns of conflicts of interest.</p>
<p>TPF attracts economic benefits as a growing industry that could drive the country’s economy.</p>	<p>TPF may put claimant litigants in a more advantageous position than defendants who are not funded by a third party and do not intend to advance a counterclaim, as funders typically support claims rather than defenses.</p>

In light of the benefits and potential drawbacks of TPF, this e-alert contends that effective regulation is crucial to maximise its benefits while mitigating its associated risks to the greatest extent feasible.

⁴ *Re Trepica Mines Ltd (No. 2)* [1963] Ch. 199, 220

How Do Various Jurisdictions Regulate TPF?

Jurisdiction	Is TPF permitted?	Is there regulation over TPF practices?
Malaysia	TPF is completely prohibited. ⁵	There is no regulation over TPF practices due to its illegal status.
England and Wales	<p>TPF activities (also known as champerty and maintenance) used to be illegal in England and Wales until the Criminal Law Act 1967 removed them from being crimes and torts.</p> <p>However, certain reservations were preserved regarding contracts contrary to public policy, with an increasing focus on justification and flexibility.⁶</p>	<p>The Association of Litigation Funders of England and Wales (ALF) facilitates self-regulation of TPF. It has a Code of Conduct which aims to protect funded litigants and manage conflicts of interest. The ALF also has protective measures such as restrictions on termination clauses in funding agreements and a complaint procedure for funded litigants.</p> <p>In 2023, the Supreme Court⁷ held that TPF agreements which provide for the remuneration of the funder based on a percentage of damages awarded are considered “damages-based agreements”</p>

⁵ The legislation and case law prohibiting TPF include the following: Section 3 of the Civil Law Act 1956, *Amal Bakti Sdn Bhd & Ors v Milan Auto (M) Sdn Bhd & Ors* [2009] 5 MLJ 95, *Mastika Jaya Timber Sdn Bhd v. Shankar Ram Pohumall (No. 2)* [2010] 10 CLJ 312, *Federal Furniture Industries Sdn Bhd v Chim Yiam Lee, Tan & Associates (Dahulunya dikenali sebagai Chim Yiam, Lee & Associates)(Disaman sebagai firma guaman)* [2012] MLJU 1629, Section 24(e) of the Contracts Act 1950, *Theresa Chong v Kin Khoon & Co* [1976] 2 MLJ 253, and section 112(1) of the Legal Profession Act 1976

⁶ This can be seen in cases like *Regina (Factortame Ltd and others) v Secretary of State for Transport, Local Government and the Regions (No 8)* [2002] EWCA Civ 932 and *London & Regional (St George’s Court) Ltd v Ministry of Defence* [2008] EWCA Civ 1212.

⁷ *R (on the application of PACCAR Inc and others) v Competition Appeal Tribunal and others* [2023] UKSC 28

		and therefore must adhere to Damages-Based Agreements Regulations 2013 (SI 2013/609).
Singapore	<p>TPF was completely prohibited until the Civil Law (Amendment) Act 2017 abolished the practice as torts.</p> <p>The Civil Law (Third-Party Funding) Regulations 2017 permitted TPF in international arbitration and related court and mediation proceedings in limited circumstances as long as the funders meet the requisite criteria.</p> <p>In June 2021, the Civil Law (Third-Party Funding) (Amendment) Regulations 2021 were enacted, extending the scope of TPF practices to domestic arbitration, proceedings commenced in front of the Singapore International Commercial Court (SICC) as well as related court and mediation proceedings.</p>	<p>The introduction of TPF in 2017 led to the amendments to the Legal Profession Act, issuance of guidance notes by the Law Society of Singapore, and guidelines for third-party funders from the Singapore Institute of Arbitrators (SI Arb) which seek to regulate TPF by qualifying third-party funders, managing conflicts of interest, defining the role of third-party funders in legal proceedings, and establishing disclosure requirements.</p> <p>Local lawyers involved in TPF agreements must abide by the Legal Profession (Professional Conduct) Rules 2015, which serve to prevent conflicts of interest. Foreign lawyers in SICC proceedings will fall under the governance of the amended Legal Profession (Representation in Singapore International Commercial Court)</p>

		Rules 2014 as a result of the 2021 TPF expansion. These rules contain provisions regarding disclosure obligations and managing of the financial interests of these lawyers in these TPF agreements.
Hong Kong	<p>TPF practices are currently torts and are also indictable offences, which could result in fines and imprisonment. However, there are three exceptions to the prohibition on TPF:</p> <ol style="list-style-type: none"> 1. Cases where the funder has a legitimate common interest in the litigation's outcome; 2. Cases where access to justice considerations prevailed; and 3. Cases in specific categories such as the sale or assignment of actions commenced in bankruptcy. <p>In 2017, an amendment of the Arbitration Ordinance permitted TPF for domestic and international arbitration.</p> <p>In December 2022, sections were added to the Arbitration Ordinance, which provides for “outcome</p>	<p>TPF agreements need to abide by the regulatory requirements under Part 10A of the Arbitration Ordinance and the Code of Practice for Third-Party Funding of Arbitration. This Code established stringent requirements for third-party funders to qualify, such as maintaining financial capacity and access to a minimum amount of capital. Managing conflicts of interest is also emphasised, with third-party funders required to have effective conflict management procedures and refrain from influencing the arbitration process. Additionally, disclosure obligations are placed on funded litigants, although details of the funding agreement are typically excluded from disclosure.</p> <p>An advisory body appointed by Hong Kong’s Secretary for</p>

Head Office

Level 6, Menara 1 Dutamas
Solaris Dutamas
No. 1, Jalan Dutamas 1
50480 Kuala Lumpur
Malaysia
Tel: +603 6208 5888
Fax: +603 6201 0122

Johor Office

Suite 21.01
21st Floor, Public Bank Tower
No.19, Jalan Wong Ah Fook
80000 Johor Bahru, Johor
Tel: +607 278 3833
Fax: +607 278 2833

Penang Office

51-12-E, Menara BHL Bank,
Jalan Sultan Ahmad Shah,
10050
Penang
Tel: +604 299 9668
Fax: +604 299 9628

Email

enquiry@lh-ag.com

Website

www.lh-ag.com

	related fee structures for arbitration” (“ORFSA”).	Justice acts as the regulatory body over ORFSAs.
--	--	--

What Should Be The Approach Moving Forward?

As legal landscapes continue to evolve, policymakers, practitioners, and stakeholders must engage in ongoing dialogue to strike a balance between justice, access, and regulatory oversight in the realm of third-party funding. Collaborative efforts on both national and international levels are imperative to address emerging challenges, uphold ethical standards, and ensure fairness in legal proceedings.

Looking ahead, it would be beneficial for Malaysia to consider legalising TPF while implementing appropriate regulations. This would involve studying regulatory models from other jurisdictions and adapting them to fit Malaysia's socio-economic and judicial landscape.

If you have any queries, please contact Pupil, **Lim Jia Yun Ruth** (jylim@lh-ag.com) or her team Partner, **Crystal Wong Wai Chin** (wwc@lh-ag.com).