Third-Party Funding in International Arbitration

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DOI: 10.55662/JADR.2024.3401

Abstract

Globalisation has created closer connections among nations. It has enabled cross-border agreements, allowing individuals from various countries to engage in commercial and non-commercial activities. Disputes between the parties in such situations are not uncommon. International Arbitration offers a straightforward, cost-effective, and efficient avenue for resolving conflicts between parties of different nationalities. This process involves selecting a neutral individual, known as the arbitrator, to resolve the disagreement according to the procedures agreed upon by the parties outside the jurisdiction of domestic courts. International arbitration offers a more impartial setting compared to local courts that adhere to the laws of a specific nation. Conversely, Arbitration Tribunals are private entities that do not comply with the laws of any particular country and can effectively handle disputes stemming from international transactions. Third-party funding refers to a practice where an outside party covers the legal costs of one disputing party in exchange for a contingent portion of any financial award received, depending on a favourable result. Although this practice is common in various regions, it is still relatively unexplored in the context of international arbitration in India. The lack of a thorough regulatory framework has created significant anxiety and reluctance to engage in such funding, making arbitration an increasingly inaccessible form of dispute resolution for many, mainly due to its perception of high costs. This paper promotes the acceptance of third-party funding in arbitration in India. It seeks to reconcile the differing viewpoints regarding the need for and extent of mandatory disclosure of such financing to establish a balanced approach that upholds the interests and rights of all parties involved. It argues for and demonstrates the need for a clear framework that requires the disclosure of such

funding while offering several provisions to respect the third-party funder's wish to remain anonymous behind the 'funding veil.' Additionally, it assesses this proposed framework in light of the recent confidentiality regulations introduced in India under the Arbitration and Conciliation (Amendment) Act, 2019 to create a practical regulatory structure by comparing it to various international practices, thereby promoting the growth of third-party funding in India in line with the country's goal to become a leading hub for international arbitration. Third-party funding is officially acknowledged in civil lawsuits according to the Civil Code of Procedure in states like Maharashtra, Gujarat, Madhya Pradesh, and Uttar Pradesh. This acknowledgement of third-party funding can be inferred from the Civil Procedure Code 1908, which regulates civil court processes in India. Amended by Maharashtra, Gujarat, Madhya Pradesh, and Uttar Pradesh, Order XXV Rule 1 of this code allows courts to secure litigation costs by requiring the financier to join the case and deposit the expenses with the court.

Meaning of International Arbitration

International arbitration, akin to litigation in domestic courts, entails the resolution of disputes by arbitrators in a manner that transcends national boundaries. This method, characterised by its consensual, impartial, obligatory, and enforceable nature, is more efficient and practical than traditional court processes. It serves as a platform for parties from diverse legal, linguistic, and cultural backgrounds to come together and settle their disagreements. International arbitration may be discretionary or mandated by including a 'mandatory arbitration clause.' Typically, parties establish 'arbitration agreements' in advance. As per Article II (1) of the New York Convention,[i] Such an agreement is "a written agreement where the involved parties commit to resolving through arbitration any present or future disputes arising from a specified legal relationship, whether contractual or otherwise." Therefore, international arbitration offers organisations involved in global transactions a neutral mechanism for dispute resolution.

Arbitration originates deeply rooted in history, albeit more informal than contemporary practices, predominantly relying on established traditions. The expansion of global trade and commerce necessitated the exploration of alternative dispute resolution mechanisms to address conflicts arising from commercial transactions. Due to its inherent characteristics, such as impartiality, adaptability, and convenience, arbitration emerged as the most dependable method for settling disputes. The inception of modern international arbitration can be traced back to the late 19th century, marked by the establishment of entities like the Permanent Court of Arbitration and the International Chambers of Commerce.

The Hague Convention of 1899 laid a solid foundation for international arbitration by introducing regulations and protocols governing resolving disputes through this method. A significant milestone in the realm of International Arbitration was the inception of the United Nations Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958), which simplifies the acknowledgement and execution of arbitral decisions transcending national boundaries, consequently reinforcing the enforceability and efficacy of international arbitration. Apart from its focus on arbitration, the convention aimed to foster global collaboration, disarmament, and amicable conflict resolution through diplomatic and arbitration means. Thus, the convention played a pivotal role in advancing international arbitration, encompassing various facets of international law and conflict resolution beyond arbitration itself. The Hague Convention also included the Convention for Pacific Settlement of International Disputes (1899), which established a framework for arbitration, conciliation, and judicial resolution of global disputes. This particular convention significantly contributed to the progression of international arbitration by standardising the regulations and procedures for resolving disagreements among nations. During the 20th century, investor-state arbitration gained significant traction with the proliferation of bilateral and multilateral investment agreements. These agreements grant foreign investors the authority to initiate arbitration proceedings against the host nation in case of treaty violations. This established the International Centre for Settlement of Investment Disputes in 1966. This institution serves as an impartial platform for settling investment-related conflicts, primarily involving investors and states, to enhance investment inflows and economic growth through fair, efficient, and unbiased mechanisms for resolving disputes arising from international investment pacts, agreements, and contracts. In response to the changing economic, political, and legal landscapes, international arbitration has evolved by embracing technological advancements, such as the progression of e-arbitration proceedings, coupled with substantial efforts to fortify transparency and efficiency throughout the arbitration process.[ii]

International Arbitration is a neutral forum for settling such disagreements, ensuring equity and objectivity. The enforceability of international arbitral decisions is straightforward; the New York Convention outlines the process for enforcing such decisions across more than 160 nations. Various international arbitration bodies exist, allowing disputing parties to access expertise from professionals worldwide to settle their disputes efficiently. These bodies boast arbitrators who possess extensive knowledge and experience in the field. International Arbitration offers a degree of adaptability regarding procedural regulations, legal options, and arbitration language, granting parties significant influence over the proceedings. This control enables them to customise the process to meet their requirements and preferences.[iii]

International Commercial Arbitration under Indian Laws

Section 2(1)(f) of the Arbitration & Conciliation Act, 1996[iv] introduces the concept of International Commercial Arbitration (ICA), arbitration in which disputes are based on the principle of commerce and application of law[v]. This legal standard is concerned with cases where any parties involved are a foreign national, foreign resident, foreign corporate entity, or any other kind of association, organisation, or individual dominated by a foreign principal. This shows that the execution and decision of any arbitration involving a foreign corporation in India is an internal matter of India's judicial system. The provisions of Part 1 of the Act apply to ICA proceedings and all arbitrations and tribunal proceedings conducted in or outside India. Nonetheless, in situations where amicable settlement proceeds from outside the Indian territory, the requirements provided in Part I of this legislation (except sections 9,[vi] 27,[vii] and 37,[viii] will not be applicable unless the dispute is to be referred to regional courts by the mutual consent of the parties. As per the judicial interpretation of section 2(1)(f)(iii)[ix] of 2015's Amendment Act, a strict interpretation would suggest that an arbitration having a place in India where the prevailing place of central management and control is the foreign nation would be: the international commercial arbitration (ICA) in question is before the enactment of 2015's Amendment Act. However, in the case of TDM Infrastructure Pvt. Ltd. v. UE Development India Pvt. Ltd.,[x] notwithstanding foreign control, the Court of India noted, "*The Act addresses arbitration concerning companies incorporated under Indian law with a majority of owners* *whose circumstances of control were outside India*." Because of this, in the context of the Act, arbitration shall be subject to international origin.

On the other hand, the Supreme Court laid down the precedent that these foreign-controlled Indian incorporated companies are domestic entities that have the right to arbitration. A new term, "a company," was underlined in Section 2(1)(f)(iii) of the 2015 Amendment Act Act, limiting the scope of this section to the ownership structure of either individuals or an organisation. Consequently, whether a local corporation has its head office overseas raises the question of central management and its anywhere-else-in-the-world or arbitration option. As a result, the question needs to be more arguable. In a specific legal matter recently surfaced in Mumbai, a group of Indian and international corporations are vying to choose the chairman, India's top authority, even though the Indian company should do so and has the upper hand. The whole corporate structure and management are located in India under the ruling of the Supreme Court.[xi]

Arbitrability stands at the crossroads of the overlapping of commercial and jurisdictional arbitration components that come into direct contact. In this regard, the critical question of the scope of the dispute that is considered permissible for arbitration and arbitrable issues is raised. Booz Allen and Hamilton Inc. v. SBI Home Finance Ltd.,[xii] The case involved a debate on the arbitrability issue, and the Supreme Court upheld its importance. It emphasised that 'arbitrability' encompasses distinct connotations across various contexts: disputes that are arbitrable, those that have an arbitration clause, and agreement-based disputes. It stated that in those cases, the Court held that the civil court could settle the dispute by mediation, and the same issue could be resolved by arbitration. On the other hand, some instances that the private tribunal cannot handle may be prohibited from arbitration proceedings. Disputes that are not capable of being arbitrated are, for example, associated with prosecution offences, divorce or marital disputes, child custody, child guardianship disputes, insolvency, and winding up issues, testamentary matters such as the issuance of probate, letters of administration, and succession certificate and eviction or tenancy disputes controlled by specialised statutes which are guarded. The arbitral instance in N. Radhakrishnan v. M/S Maestro Engineers[xiii]
This is to light the fact that when allegations of wilful fraud and serious malpractices arise, the resolution of such issues should be dealt with by the court rather than the arbitrator because of his/her criminal nature.

The court continued to point out that an arbitrator, a product of the contract, has limited authority. In contrast, the judiciary is more appropriate for dealing with rough and finer disputes and providing various remedies to the parties. It has been an opposite turn of events for the Supreme Court's ruling in Swiss Timing Ltd. v. Organizing Committee, Commonwealth Games 2010, Delhi,[xiv] Towards the case of Swiss Timing Ltd. v. Organizing Committee, Commonwealth Games 2010, Delhi, which has overruled the legal principle previously explained in the N. Radhakrishnan case. In the same way, another relevant/noteworthy case is the situation involving World Sport Group (Mauritius) Ltd. v. MSM Satellite (Singapore) Pte. Ltd. clarified that accusations of fraud do not prohibit the referral of parties to arbitration seated in a foreign jurisdiction unless specified in Section 45 of the Act,[xv] Such as instances where the arbitration agreement is deemed null, inoperative, or impracticable. Thus, though accusations of fraud may hamper arbitration in Indian-seated cases, this limitation does not cover the cases that occur in foreign-seated disputes.

For the first time, the Supreme Court did render its landmark judgment in A Ayyasamy v. A Paramasivam & Ors wherein it was construed that no proceeding against straightforward misrepresentations of facts would be admissible, only those new categories of frauds which are undisguised would be exceptions.[xvi] In the case of A Ayyasamy, the Supreme Court observed that the verdict in Swiss Timing did not nullify Radhakrishnan and established that:

- Instances of fraud concerning ordinary facts will undergo arbitration, whereas representatives of noteworthy personages and individual qualities will not.
- Unless the fraud has been raised as part of the dispute, there is nothing in principle unlawful in dealing with the arbitrability of the scam.

The provisions bring about an exception between 'fraud simpliciter' and 'serious fraud' and conclude that while the prior is more appropriate to be adjudicated by a court, the latter can still be deliberated on at the level of an arbitral tribunal. Asymmetrically, the Supreme Court has acknowledged that an appointed arbitrator is sufficient to investigate the fraud charges.[xvii] In the case of GMR Energy Ltd. v. Doosan Power Systems India Pvt. Ltd. & Ors.,[xviii] The Delhi High Court recognised that its previous verdict in Sudhir Gopi v. Indira Gandhi National Open University[xix] was per incuriam, as it was issued without taking into account the Supreme Court's decision in A Ayyasamy, where the Court outlined situations that are not arbitrable. The court determined that an arbitral tribunal can adjudicate matters concerning alter ego. Subsequently, in the case of Rashid Raza v. Sadaf Akhtar,[xx] the Supreme Court referenced its judgment in A Ayyasamy. It established operational criteria for assessing the arbitrability of fraud allegations when appointing an arbitrator under Section 11 of the Act.[xxi] It identified two criteria from A Ayyasamy to differentiate between a mere fraud allegation and other matters:

1. "*Whether the claim impacts the entire contract and especially the arbitration agreement, rendering it null or*
2. *if the fraud accusations involve the internal relationships of the parties without affecting the public domain*."

The Supreme Court, in the case of Vimal Shah & Ors. v. Jayesh Shah & Ors.,[xxii] Determined that issues connected with trust documents and the Indian Trusts Act of 1882 are inappropriate for arbitration. In the case of Suresh Shah v. Hipad Technology India Pvt. Ltd.,[xxiii] Conflicts arose due to a sublease agreement that contained an arbitration clause. The Supreme Court received an application for the selection of an arbitrator according to Section 11 of the Act. Before addressing the appointment question, the Court reviewed whether lease/tenancy agreements/deed disputes could be arbitrated. It maintained that eviction or tenancy disputes are unsuitable for arbitration, especially those governed by specific provisions that safeguard renters from eviction and assign a particular court with jurisdiction.

In 2019, the Supreme Court, in the case of Vidya Drolia & Ors. v. Durga Trading Corporation,[xxiv] Durga Trading Corporation referred the matter of the arbitrability of the landlord-tenancy disputes to a bench of three judges. The Court determined that a dispute would be non-arbitrable if:

a) Undetermined actions are based on everything the judge has to judge and something other than the subordinate personal property rights associated with rem.
b) Third parties' rights are included, erga omnes consequences result, and centralised adjudication is required. This combination forces us to realise that mutual adjudication is improper and infeasible.
c) It is aimed at the states' most transcendental issues, sovereignty & "the community's general interests.
d) Statutory direct prohibition against arbitration agreements can be done explicitly or typically indirectly.

The Court decided that disputes arising from tenancy agreements are proper for arbitration and may be excluded only under the general provisions of relevant law. The Apex Court believed that when it comes to the arbitrability of the dispute, the arbitration tribunal shall be the authoritative forum to examine and settle all the relevant issues. The Supreme Court considered an analogous question in the case of N.N. Global Mercantile Pvt. Ltd. V. Indo Unique Flame Ltd. & Others (Global Mercantile).[xxv] After the decision in the Vidya Drolia case, whether arbitration might be used to settle the matter of a fraudulent invocation of a bank guarantee was one of the main issues the Supreme Court examined in the Global Mercantile case. In upholding the dispute's arbitrability, the Supreme Court approved the fraud standards and relevant examination procedures in the court's earlier rulings in Vidya Drolia and Rashid Raza. It has been established through a series of Supreme Court rulings that fraud allegations are admissible in civil dispute arbitration procedures. There is, however, one exception to this generalisation. According to this exception, arbitration cannot be used when fraud undermines and nullifies the arbitration provision itself.

Introduction to Third-Party Funding and Treatment in Various Jurisdiction

International commercial arbitration functions as a mechanism for resolving disputes between private parties involved in international commercial agreements rather than serving as an alternative method. While not entirely new, third-party funding (TPF) is a relatively innovative development. TPF has become one of the fastest-growing and most debated topics within international commercial arbitration. It occurs when a third-party funder, who is not a party to the dispute, agrees to cover some or all of the arbitration costs for one party in exchange for a predetermined percentage of any recovery. If the arbitral tribunal issues an unfavourable decision against the funded party, the funder risks losing their investment. This funding typically covers legal expenses, including fees for lawyers, experts, external counsel, and other costs associated with the arbitration process. Entities providing TPF include insurance firms, investment banks, hedge funds, and legal representatives or client's legal practices. Third-party funding in international commercial arbitration is a timely and contentious issue. It involves a third-party entity providing financial support—either partially or fully—for the arbitration expenses of one of the parties involved. If a favourable decision is reached, the funder typically receives compensation equivalent to an agreed-upon percentage of the awarded amount. However, if the decision is unfavourable, the funder risks losing their initial investment. One of the main concerns regarding the involvement of third-party funders in arbitration is the

ISSN 2583 682X
Volume 3 Issue 4 – October- December 2024

potential for conflicts of interest among arbitrators, primarily due to a lack of transparency about these funders' roles in the process.

Third-party funding has predominantly been considered valid and lawful. This conclusion can be drawn from instances such as Arkin v. Borchard Lines Ltd.,[xxvi] where the English Court of Appeal demonstrated a supportive stance towards third-party funding to access unattainable justice. This stance was reaffirmed by the High Court of Australia in Campbell Cash & Carry Pty Ltd. v. Fostif Pty Ltd.,[xxvii] emphasising that litigation funding does not violate public policy or exploit due process. This represents a notable shift in common law jurisprudence from past efforts to invalidate third-party financing, as evidenced in the case of Re Trepca Mines,[xxviii] where Lord Denning cautioned against the risks posed by third parties in litigation, suggesting that such entities may be tempted to manipulate damages, withhold evidence, or even influence witnesses for personal gain. In the Indian jurisdiction, third-party financing has frequently been deliberated within legal disputes, particularly civil lawsuits. This aspect is notably highlighted in the ruling of the Privy Council on an appeal originating from the High Court of Calcutta in the matter of Ram Coomar Candoo v. Chunder Canto Mukherjee.[xxix] The ruling emphasised that a reasonable agreement to provide financial support for a legal case in exchange for a portion of the recovered assets does not violate public policy or legality. Nevertheless, such agreements must be subject to thorough scrutiny, mainly when they exhibit elements of being excessively demanding, unethical, or pursued for inappropriate purposes, as they should then be deemed null and void. Furthermore, third-party funding is formally acknowledged for civil lawsuits in the Code of Civil Procedure under Order XXV Rule 1,[xxx] which authorises courts to obtain litigation costs from a funder by involving them as a party and resolving the costs judicially. A recent ruling by the Supreme Court arose in the case of In Re GA Senior Advocate,[xxxi] where it was established that a third-party financing arrangement linking returns to the case's outcome is not inherently unlawful unless the third party acts as the legal representative. Consequently, the bench effectively prohibited legal professionals from assuming the role of the third-party financier who agrees to fund the legal proceedings based on a contingency or success-dependent fee.

Concept of Third-Party Funding

In recent years, we have observed a notable surge in financial activities primarily centred on investor-state arbitration, subsequently expanding towards international commercial arbitration. In contrast to domestic litigation, where judges appointed by the court resolve disputes, arbitrators appointed by the involved parties settle investor-state or commercial disputes. Third-party funding represents a financial approach whereby an external entity not engaged in the specific dispute provides funding for legal fees of one party or covers any orders, awards, or judgments issued against that party, or both. This financing method proves highly advantageous to clients as it enables them to pursue a claim while transferring the financial burden and risk of loss entirely to the external funder. The involvement of a third party in providing financial support to a litigant occurs when said party has no direct connection to the legal dispute; in exchange, the third party receives a portion of the proceeds if the claim is successful or nothing if the claim fails. This type of funding is recognised under various terms like claim, alternative, and third-party litigation funding. A funding decision made by a third-party funder is purely viewed as an investment. Having no affiliation with the dispute, the funder inserts itself into the scenario by advancing funds.

The evolution of the market has led to an expansion in the variety and complexity of available funding products and structures. It is important to note that there is no universal solution, and the description above represents the most fundamental aspect of funding. Third-party funding, commonly known as "litigation finance," has significantly advanced. Besides supporting individual cases, litigation finance is now utilised for a more comprehensive array of objectives, leveraging the proceeds from litigation or arbitration as collateral. A recent trend involves the emergence of portfolio funding, where financiers offer a comprehensive funding package for a collection of cases. While third-party funding provides substantial benefits, such as enhancing access to justice, it also presents certain risks and obstacles, such as concerns related to conflicts of interest, disclosure, and cost security. The recent proliferation of third-party funding within international arbitration, coupled with ongoing discussions on this subject, has instigated noteworthy progress in its regulation at national and global levels.

The issue of third-party funding in international commercial arbitration stands out as one of the field's most current and contentious topics. For those considering financing on a case-by-case basis, a preliminary checklist can be beneficial: Funders are inclined to support cases involving damages, as their returns are tied to the recoveries achieved, making claims with a damages outcome the primary focus. Consequently, funding is typically accessible to claimants or defendants with a counterclaim. Unless specialising in more minor claims, funders generally support individual cases where potential damages exceed £10 million. Investing in an arbitration matter carries substantial risk, requiring funders to assess the investment-to-quantum ratio, usually demanding a minimum damages outcome of £10 million. Funders seek promising success prospects, evaluating their claim before committing to funding, ensuring confidence in its viability and progression.

When considering funding, funders will inquire about the respondent's ability to satisfy the claim, costs, and interest, particularly in cases involving states, assessing their track record regarding arbitration award payments. Additionally, funders will seek information on the location of assets, as enforcement risk plays a critical role in their decision-making process. Challenges related to enforcement in jurisdictions with limited enforcement capabilities may dissuade specific funders. Factors such as the respondent's willingness to continue the legal battle can also impact the funder's decision. The arbitration's seat holds significance, as it dictates the permissibility of funding under local legislation. Moreover, the enforcement location carries weight, as the revelation of funding may be used to raise public policy concerns to obstruct enforcement.

Various scenarios may emerge when enforcing arbitral awards when the claimant has received funding from a third party. The enforcement of agreements for third-party funding and arbitration awards involving a third-party funder may vary depending on the jurisdiction where the award or funding agreement is being enforced. Some of these situations include:

The seat of arbitration

In cases where an award is necessary at the place of arbitration, the feasibility of such enforcement would rely on the jurisdiction of the arbitration site and its regulations concerning the validity of third-party funding arrangements is illustrated by the Irish Supreme Court ruling in Persona Digital Telephony Limited & Sigma Wireless Networks Limited v The Minister for

Public Enterprise, Ireland, and the Attorney General.[xxxii] In this case, the court determined that such agreements could violate national public policy. The court concluded that the third-party funding arrangement compromised the arbitration award, rendering it subject to annulment under Irish law. However, it is essential to note that international arbitration increasingly embraces the practice of third-party funding.

In the case of Giovanni Alemanni v. The Argentine Republic,[xxxiii] The tribunal's decision on Jurisdiction and Admissibility, dated November 17, 2014, expressed that "*the practice [of third-party funding] is by now so well established both within many national jurisdictions and within international investment arbitration that it offers no grounds for objection*." Ben Knowles and Paul Baker highlighted several risks associated with enforcing funded arbitral awards in an anti-funding environment. The article examines the enforcement of arbitration awards in cases involving third-party funders in jurisdictions where such funding is not allowed.[xxxiv] In these areas, courts may reject the enforcement of funded awards. A key question for countries parties to the New York Convention is whether these actions are permissible. The authors argue that signatory states are generally required to enforce arbitral awards, with enforcement refusal limited to specific grounds. The primary potential justification for denying enforcement would be public policy concerns. Whether countries sceptical of third-party funding will establish legal precedents on this issue remains to be seen.

Thus, the consensus regarding the challengeability of arbitration awards in a jurisdiction influenced by third-party funding agreements is lacking. Some rulings support the enforcement of awards under the New York Convention, a stance endorsed by prominent scholars. Conversely, the Irish Supreme Court case referenced above demonstrates a nation's ability to reject award enforcement solely due to involvement in third-party funding. Despite potential discouragement to funders, global trends suggest increasing acceptance and legitimacy of such funding arrangements shortly.

Third-party funding agreements executed in the claimant's place of residence

In this scenario, the claimant enters a third-party funding agreement with legal validity in their jurisdiction. However, questions arise regarding this agreement's validity when the award enforcement occurs in a different jurisdiction. In a recent ruling by the English Court in Essar Oilfields Services Limited v Norscot Rig Management Private Limited,[xxxv] The claimant was allowed to recover legal expenses through funding from a third party. A Scottish firm had established a third-party funding agreement to support the arbitration against Essar, which the arbitral tribunal deemed legal—a decision the English Court also upheld during the award enforcement process. This case suggests that the validity of the third-party funding agreement in the claimant's jurisdiction strengthens its legitimacy. Additionally, it is essential to note that English courts are increasingly adopting a pro-arbitration stance. Therefore, the award's validity will depend on the approach taken by the court responsible for executing the arbitration award—the validity of the third-party funding agreement and the arbitration award in the execution jurisdiction. Upon examining the aforementioned judicial decisions and scholarly works, the jurisdiction where the arbitration award is enforced should recognise third-party funding agreements as legally valid. While a third-party funding agreement may be legally enforceable in the jurisdiction where it was established, the court responsible for enforcement may overturn an award if said jurisdiction does not acknowledge the legitimacy of such agreements. Prominent scholars and experts in international arbitration have expressed the view that adherence to the principles of the New York Convention should serve as the primary guiding principle in enforcing these awards. A restrictive interpretation should permit the enforcement of such awards without national courts imposing limitations based on their respective laws governing third-party funding agreements.

Types of Third-Part Funding

In standard or traditional Third Party Funding (TPF), a person or company seeks financial support from a funder to manage legal expenses or liabilities emerging from a dispute.[xxxvi] In exchange for funding, the party receiving support may offer a portion of the award contingent

ISSN 2583 682X
Volume 3 Issue 4 – October- December 2024

upon a favourable outcome. Typically, the return percentage varies from 20-40% or may equate to around three times the amount invested, depending on which is more significant.[xxxvii] In the event of an unfavourable outcome, the obligations of both the funder and the funded party are determined by the conditions outlined in the TPF Agreement ('TPFA'). Within international arbitration, clients receiving funds can be either claimants or respondents, and the experiences for both categories are generally similar. Initially, the client compiles a list of potential funders and applies for financial support, either exclusively or concurrently. To evaluate the claim, the party requesting funding must supply detailed information about the claim to prospective funders. At the same time, the funder and the client will enter into a Non-Disclosure Agreement ('NDA') to safeguard the confidential information exchanged. Subsequently, the funder utilises its expertise to conduct due diligence, which assists in evaluating the likelihood of success based on merits, the strengths and weaknesses of the claim, the capacity to recover the award from the opposing party, settlement prospects, client creditworthiness, and other relevant factors. The due diligence process may also involve assessments by external advisors to the funder, such as legal consultants, auditors, or specialists in quantum valuation. For claims of high value or significance that seek considerable funding, the due diligence process could extend over several months and involve substantial costs, with the responsibility for these expenses dictated by the funder's policy. If the funding is approved, the funder and the funded parties negotiate the terms of the agreement, which encompass the level of control the funded party will retain, the types of expenses covered by the funder, the percentage of the award to be received in case of a successful outcome, and other complexities like scenarios permitting the funded party to terminate the funding. This section mainly concentrates on the alternatives to the conventional form of TPF. Numerous types of TPF exist, but for clarity, the primary and most recognised forms of funding will be emphasised alongside their key distinctions.[xxxviii] To comprehend the kinds of TPF, one must be familiar with the three core stakeholders involved in the TPF process and their respective interests, which will be elaborated below.

The Three Stakeholders in TPF

Third-Party Funder

A funder is any individual or organisation providing financial support or other resources for the prosecution or defence of a case and having a vested financial interest in the outcome of arbitration or litigation. For funders, international arbitration presents an appealing investment opportunity due to the significant claim values, the expedited nature of the proceedings, the reduced evidentiary costs, and the expertise of the individuals making decisions. Additionally, there is a higher degree of outcome predictability and a strong likelihood that awards will be enforceable, making the industry attractive to funders. Funders prefer to keep their identities hidden from the opposing party and the tribunal to safeguard their interests concerning the funding agreement and to avoid delays in the proceedings that could arise from conflicts of interest between the funder and the arbitrator, which might lead to challenges against the arbitrator's appointment.

Funded Party

The party that requests financial support from an external source is the funded party. This party may seek financial assistance for various reasons, primarily to alleviate losses incurred due to the dispute. Different categories of parties might require funding, including major corporations, legal firms, individuals, and occasionally, even sovereign states. Typically, the funded party initiates the claim (the claimant), though there are instances where third-party funding is pursued by the respondents as well. One reason for the prevalence of funding for claimants is that third-party funding is generally based on strong claims rather than counterclaims, which are less frequently made. Throughout the arbitral proceedings, the funded party usually desires to maintain maximum control over how the proceedings are managed and aims to make independent settlement decisions. This interest is particularly critical because, since a third party provides the financing, it is quite possible that the funder's financial choices, such as those related to settlement offers, could heavily influence the funded party. In this scenario, the interests of the funded party may be jeopardised due to their diminished bargaining power and limited financial capabilities to continue with the dispute. Therefore, preserving a certain level of decision-making autonomy is a primary concern for the funded party. Furthermore, the funder may sometimes decide to terminate the funding agreement based on the choices made by the funded party regarding the proceedings (for instance, by accepting a settlement offer from the opposing side). This could leave the funded party in a precarious position, having already invested in the claim but lacking the financial resources to pursue it. Consequently, the funded party strives to guarantee that the funder does not possess the authority to terminate the funding agreement abruptly.

Opposite Party

The party against which the funded claim is filed is the respondent. In the context of third-party funding (TPF), the respondent may request to reveal the identity of the funder to confirm that there are no potential conflicts of interest between the funder and any member of the arbitration panel, thereby maintaining the required standards of impartiality and independence for the tribunal. Additionally, the opposing party seeks to ensure that there are no risks concerning the efficiency of the proceedings or the potential enforceability of the award at a future point due to the involvement of a funder.[xxxix]

Types of Funders

Various forms of funding exist that combine elements from the options outlined below. The party seeking funding may choose a funding agreement based on their financial needs and the level of control they wish to maintain. To enhance the reader's understanding, a brief overview of the four central and distinct types of Third Party Funding (TPF) is provided:

1. Insurance
2. Attorney Financing
3. Loans
4. Assignments

Insurance

Legal insurance represents one of the oldest alternatives to TPF. In the realm of litigation or arbitration, legal insurance functions similarly to TPF. A claimant might view insurance as a viable option since the premiums tend to be significantly lower than the typical returns expected by funders. Generally, standard premium rates are between 30-50% of the overall claim or the insured sum and are often payable upfront. Legal insurance is typically divided into legal expenses insurance and liability insurance. Both types of insurance can be acquired either before or following the occurrence of the dispute.

Legal Expenses Insurance: It is typical for companies to obtain insurance policies that cover the legal expenses related to future claims contested by the insured. This type of insurance is called ‘before the event' (BTE) insurance. With BTE insurance, the insured pays regular premiums and, in exchange, is eligible for legal expenses that may arise from future disputes. In this context, legal expenses usually include costs associated with initiating or defending a claim and fees for lawyers, arbitrators, and specialists consulted for or during the proceedings. Conversely, insurances acquired ‘after the event’ (ATE) are those taken out once a legal dispute has occurred. In such cases, the insurer requires a fixed, regular premium determined based on the anticipated legal expenses. ATE insurance aims to safeguard the insured from possible losses related to the dispute, like covering their costs (incurred while pursuing the case) or potential adverse costs.

Liability Insurance: Liability insurance, or outcome policies, are organised similarly to standard insurance agreements, where the insured is safeguarded against liabilities arising from disputes and, in exchange, pays a premium to the insurer determined by the likelihood of incurring a loss. There are two categories of liability insurance — traditional liability insurance and the modern ATE-BTE type. The key distinction between these two lies in the degree of control a funded party has. In conventional liability insurance, the insurer must defend the insured throughout the proceedings (thus primarily covering legal expenses) and indemnify the insured in an unfavourable ruling. Traditional liability insurance is not classified as TPF since the insurer acts as a co-client of the insured during the proceedings or takes over (through the right of subrogation) on behalf of the funded party while advancing the claim. By exercising the right of subrogation, the insurer assumes the position of the funded party and pursues the claims in its name. Outcome policies or traditional liability insurance are predominantly used to shield respondents from their risk liability arising from ongoing litigation or arbitration. These policies entail a considerable risk for the insurer; hence, a substantial exchange of information between the funder and the funded party is necessary, followed by a thorough (and costly) evaluation of the case to safeguard its financial interests. Regarding control, a significant drawback of traditional liability insurance is that it often requires the insured to forgo much or complete control over the management of the case and any potential settlement discussions or agreements. Typically, the extent of the insurance company's power corresponds directly to its financial involvement. In contrast, under modern ATE-BTE liability insurance, the funder does not exert any control over the management of arbitration proceedings and does not influence settlement agreements.

Attorney Financing

In success-based legal fee arrangements, the lawyer commits their resources and expertise to the case, with payment contingent on the outcome. Depending on the agreement, the lawyer may receive a diminished or no payment if the case is unsuccessful. Conversely, the lawyer might be entitled to a higher fee or an additional percentage if the claim succeeds. These potential outcomes are categorised as contingency or conditional fee arrangements. In attorney financing, the relationship between the lawyer and the client is direct, with the client maintaining complete control or management of the case, similar to an individual funding their dispute. Success-based fees can be structured as a contingency or a conditional arrangement. In contingency fee arrangements, the attorney does not collect any payment if the claim does not succeed. Generally, the fee is calculated as one-third of the damages gained from a settlement and between 40-50% of damages awarded through legal proceedings. Contingency fees encourage clients to pursue their claims, as they do not face the financial burden directly. Law firms sometimes seek loans from external funders to alleviate the financial strain that can arise from contingency fee agreements.

A conditional fee arrangement resembles a contingency fee arrangement, with the key difference being that in the former, the attorney receives a reduced fee if the outcome is unfavourable. If the client prevails, the attorney is compensated with an additional fee beyond the standard (agreed-upon). The main difference between conditional and contingency fees is that the risk of loss is shared between both parties in the former, whereas in the latter, the attorney assumes all the risk. Conditional fee arrangements ensure that the attorney is compensated for their work.

The client controls case management under attorney financing and success-based fees while the attorney takes on most of the risk. This differs significantly from traditional liability insurance, where the insurance company typically has complete control over the claim. The primary reason for this variance in control is due to the ethical obligations and conduct codes that require attorneys to diligently advocate for the case, even in circumstances where they may believe it is unwinnable. In contrast, the insurance company does not have such obligations, allowing them to withdraw the claim regardless of the insured's interests.

Loan Agreements

Individuals involved in legal disputes may choose to secure loans from banks or other lending institutions to obtain funds for defending their position or pursuing claims. Additionally, a client might receive financing from an attorney or a law firm. Moreover, the attorney or law firm could also pursue a loan to manage the gap between their current operational costs and the anticipated revenue from regular or success-based fees. The key benefit of choosing a loan is that the client maintains oversight and control over the dispute. On the other hand, the drawback is that the party receiving the funding forfeits the opportunity to lessen losses, as the amount paid under the loan agreement must be repaid regardless of the case outcome.

Assignment of Claims

The assignment of claims is pertinent to the current discussion as it has historically been viewed as a form of maintenance. In certain jurisdictions, the degree of control exerted by the funder is considered when determining the legitimacy of the funding agreement. Therefore, in most jurisdictions, traditional TPF entails the transfer of the proceeds from a successful claim rather than the right to bring forth the claim to adhere to that region's ethical guidelines and legal standards. In other jurisdictions, the assignment of claims can occur either through the complete sale of the right to pursue the claim or when a significant corporate change arises due to a merger or acquisition, asset sale, or bankruptcy liquidation. An outright sale of claims occurs in return for immediate financial compensation. In this scenario, the agreed-upon purchase price of the claim is typically lower than the claim's anticipated value. The assignment of claims resembles debt collection agreements in which an original creditor sells the debt to a third-party agency for less than its worth. In this context, a relevant contemporary case within the Indian framework is the previously referenced HCC-Blackrock deal, where HCC assigned its claims to the global investment firm Blackrock in exchange for immediate monetisation. This step was taken to reduce the company's debt and address the asset-debt mismatch challenges

HCC was experiencing.[xl] This assignment of claims arrangement is deemed vital for lowering HCC's debt and generating liquidity for financial recovery, as stated by their Group CEO, Arjun Dhawan.[xli] Another instance of assignment of claims can be found in TPF for class actions, where claimants assign their claims to a non-profit organisation that pursues the claim on behalf of the class or group of individuals seeking a settlement or legal recourse.

The various types of funding outlined in this section have developed over the years, and their validity is contingent upon the laws of their respective regions. As highlighted throughout the section, the level of control held by the funder is a critical factor in the TPF process as it reflects the interests of the involved parties. The funded entity typically favours agreeing, allowing maximum independence. Analysing the types of TPF reveals that a funder might be more inclined to engage in modern insurance policies instead of traditional ones. Furthermore, even though the funded party enjoys the necessary decision-making independence in loan agreement cases, it may shy away from it due to the relatively heavy financial obligation. Concerning attorney financing, the financial strain is minimal, and the control remains with the funded party; however, the funded party's portion of the award is significantly diminished as a considerable portion goes to the attorney or legal fees.

Benefits

Third-party funding (TPF) aids parties in arbitration by covering their legal expenses, ensuring that justice is accessible for those who lack sufficient resources. The costs associated with arbitration, such as administrative fees, attorney charges, and arbitrator fees, can be considerable, making TPF a vital mechanism for addressing financial obstacles. It serves two categories of stakeholders: those with limited resources and those with ample financial means. TPF creates a level playing field for parties facing financial hardship, enabling them to compete reasonably even with constrained budgets. Funders meticulously evaluate claims before committing their funds and provide specialised legal assistance, enhancing the likelihood of a favourable outcome. Additionally, well-capitalized companies utilise TPF to manage their financial exposure during high-stakes arbitration, thus avoiding direct liability for unpredictable expenses. TPF ensures equitable competition and promotes arbitration for individuals and businesses by redistributing financial responsibilities to third-party investors. Ultimately, it improves access to justice and provides a strategic financial approach for claimants looking to reduce risk while pursuing their legal actions.[xlii]

Challenges

In a TPF setup, an external financial backer who is not involved in the arbitration agreement develops a stake in the outcome of the case, introducing certain risks to international commercial arbitration (ICA). The funder's primary objective is profit rather than altruism, which concerns the arbitration process and the enforcement of awards. The main challenges associated with TPF in ICA include imbalanced terms and dominance by funders, potential conflicts of interest, the promotion of frivolous claims, issues with disclosure that can impact costs, and threats to confidentiality and privilege. Clients and attorneys must thoroughly evaluate these risks before entering into TPF agreements to ensure they make well-informed choices.

Unfair Terms and Dominance Over the Claim

Before entering a TPF agreement, the funder conducts due diligence and negotiates terms with the claimant. Given their financial leverage, funders might impose unfavourable conditions, such as taking a significant portion of the award or exerting influence over the proceedings. Since the funder's profit hinges on a favourable outcome, they may sway critical decisions, including the choice of legal representatives and arbitrators. Additionally, lawyers might align themselves with funders for future business prospects, which could jeopardise the claimant's interests. Although funder involvement in choosing arbitrators can benefit less experienced claimants, transparency issues remain significant.

Conflict of Interest

In commercial arbitration, arbitrators must maintain independence and impartiality, as international standards and regulations mandate. Arbitrators must reveal any potential conflicts of interest that might compromise their neutrality. A conflict of interest occurs when an arbitrator has connections to a third-party funder, such as serving as legal counsel for a company financing the claim. This situation can lead to challenges against the arbitrator's appointment, resulting in delays in proceedings and increased expenses. Similar problems arise when attorneys from the same firm represent the party receiving funding and the funder. Such conflicts jeopardise the integrity of arbitration and could ultimately lead to the arbitral award being annulled under the New York Convention.[xliii]

Frivolous Claims and Discourage Settlements

While third-party funding (TPF) improves access to legal remedies, it might also promote baseless claims. Nonetheless, this worry is chiefly misplaced since funders thoroughly evaluate cases before committing funds, with only 5–10% of claims being approved for financial support. Another concern is that TPF might deter settlements, given that the party receiving funding holds no financial risk. Funders usually favour prompt settlements to guarantee returns rather than delaying uncertain results. The threat of enforceability issues further motivates parties to seek early resolution. Nonetheless, conflicts may emerge if the funder's definition of a 'prompt settlement' does not match the expectations of the funded party, which could result in disagreements regarding claim management.

Disclosure of Third-Party Funding Agreements and the Concern of Costs

One major issue in TPF arbitration is the absence of disclosure, which may result in conflicts of interest and raise concerns about the financial stability of the funded party. Arbitration depends on the neutrality and objectivity of the tribunal, which can be undermined if the involvement of a funder is undisclosed. The tribunal may require cost security if a party cannot pay an adverse award. However, not all funded parties lack funds—many financially healthy companies utilise TPF to mitigate risk. The determination of security for costs should reflect financial capability rather than simply the existence of a funder. Furthermore, the typical approach in arbitration for cost allocation adheres to the "loser pays" principle. Still, the significant Essar Oilfields ruling established a precedent for recovering a funder's expenses. This case underscores the ongoing discussion regarding ownership and financial liability for claims in international commercial arbitration.

The Concern of Confidentiality and Breach of Privilege

Confidentiality is a crucial aspect of international commercial arbitration, safeguarding the privacy of case-related information. However, pursuing third-party funding (TPF) can jeopardise this confidentiality. To evaluate the feasibility of an investment, funders analyse important arbitration documents despite not being legally bound by confidentiality agreements. This exposure raises the possibility of exploiting sensitive information against the non-funded party in subsequent legal conflicts. Another significant issue is the potential violation of attorney-client privilege. The party receiving funding may be required to disclose privileged communications to the funder, which can blur the boundaries of legal protections. Funders may also gain access to confidential documents created by the party's legal counsel, which could weaken the attorney-client privilege. These concerns underscore TPF's difficulties preserving confidentiality and legal privilege in arbitration.

Third-Party Regulation and the Supportive Role of Arbitral Institutions & Soft Law Instruments

Firstly, there is a concern about the risk of "over-regulation," which could impose unnecessary constraints on using third-party funding. Secondly, domestic regulations often vary across different jurisdictions, creating opportunities for "forum shopping," where parties select a governing law that is either favourable or silent on specific issues. Thirdly, due to the complex nature of problems surrounding third-party funding, it is difficult to address them comprehensively with a single set of definitive rules, as these issues can vary significantly from case to case and jurisdiction to jurisdiction, evolving alongside the practice and perception of third-party funding. The idea of a universal solution is impractical, underscoring the need for flexibility. As a result, the roles of arbitral institutions and international guidelines have become increasingly important in enhancing effectiveness in this area. Institutional arbitration rules offer broader applicability than domestic laws and are specifically tailored for arbitral processes. Meanwhile, international guidelines, although non-binding, provide valuable flexibility. For instance, the 2014 International Bar Association Guidelines on Conflicts of Interest were among the first to address third-party funding, offering helpful guidance to practitioners and proving effective. Hence, the recommendation is to avoid a fragmented system of national regulations on third-party funding in favour of developing non-binding guidelines for practitioners in navigating issues related to third-party funding in international arbitration.[xliv]

Maintenance involves providing financial support to a claim holder, enabling the pursuit of the claim legally even when the provider has no valid interest in the claim. Champerty further stipulates that the provider has a direct financial stake in the claim's outcome, offering money in exchange for a share of the damages if the claim succeeds. The rationale behind prohibiting these practices due to ethical and moral concerns and their illegality can be elucidated through specific quotations. Historically, within common law jurisdictions, the concepts of ‘maintenance’ and ‘champerty’ were established to prevent the financing of lawsuits by external parties. This was primarily to avoid unjust enrichment of third parties without genuine interests in the litigation, as it was feared that this could lead to frivolous or harassing lawsuits. However, many jurisdictions have taken a more practical approach toward third-party funding in pursuing enhancing access to justice. In certain jurisdictions like Ireland, maintenance and champerty are still classified as wrongful acts and criminal offences. For instance, in May 2017, the Irish Supreme Court prohibited a third-party funder from supporting a significant case against the Irish government, citing champerty. Nevertheless, Asian attitudes towards third-party funding are evolving, with Hong Kong and Singapore enacting laws to allow and regulate such funding in international arbitration.

Legislation in various jurisdictions must clarify the permissibility of third-party funding, especially in arbitration, leading to uncertainty about the judicial stance on such funding agreements in arbitration proceedings. In jurisdictions where third-party funding is permitted, regulations may differ for funders and are approached in varied ways. Below, we outline the regulatory frameworks for third-party funders in England and Australia. In England and Wales, there is no formal regulation of third-party funding; instead, self-regulation is encouraged by adopting a code of practice. The Code of Conduct for Litigation Funders was finalised in November 2011, and the Association of Litigation Funders of England and Wales was established. This Code is obligatory for all association members and governs funding “*litigation, arbitration, or other dispute resolution procedures*.” In Australia, lawyers are prohibited from receiving contingency fees, preventing them from having a financial stake in their clients’ awards. However, external third-party funders are allowed to participate in litigation and arbitration. To address frivolous or vexatious litigation, court regulations in each jurisdiction and common law principles empower courts to protect the administration of justice by issuing orders regarding procedures, including oversight of arbitral processes, to prevent legal system abuse by litigation funders.

Currently, there are no specific regulations governing the capital adequacy of third-party funders in Australia unless they choose to obtain a financial services license, which is not mandatory. This exemption arises because the law excludes litigation funders from being classified as managed investment schemes, provided that the funding agreement includes adequate measures to manage potential conflicts of interest. The funder's senior management must document, implement, monitor, and oversee these measures under regulatory guidelines.

Latest Developments in Third-Party Funding Regulation & Emerging Issues

Singapore

On January 10, 2017, the Singapore Parliament passed the Civil Law (Amendment) Act (Bill No. 38/2016), which took effect in March 2017. This legislation amends Singaporean law to permit third-party funding in international arbitration and related judicial proceedings, subject to specific conditions, including eligibility criteria for funders. Before this change, third-party funding was prohibited in Singapore, and restrictions on funding for state court litigation remained in effect.

Because of the recent legal changes in Singapore, the 2017 Investment Arbitration Rules (applicable from 1 January 2017) of the Singapore International Arbitration Centre (SIAC) confer upon an arbitral tribunal the authority to demand disclosure of any funding arrangement concluded by one of the parties involved in the proceedings, as well as information regarding the third-party funder implicated, along with additional details concerning the funder's engagement and stake in the case's outcome. On 31 March 2017, SIAC released a Practice Note on Arbitrator Conduct in Cases Involving External Funding, outlining guidelines on best practices and ethical standards to assist arbitrators in navigating issues related to their independence, impartiality, disclosure obligations, and the management of costs.

Hong Kong and Singapore are at the forefront of explicitly regulating third-party funding in international arbitration at the governmental level. Before these legislative changes, third-party funding of legal proceedings was banned entirely in both jurisdictions due to the common law doctrines of maintenance and champerty. The new laws permit third-party funding in specific contexts and require disclosure of such funding arrangements and identification of the involved funders. Such regulations at a national level represent a novel development in the realm of arbitration.[xlv]

Hongkong

Hong Kong has officially endorsed third-party funding for arbitrations held within its jurisdiction by enacting the Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Bill 2016, which took effect on June 14, 2017. This development parallels similar legislative changes in Singapore aimed at regulating previously prohibited third-party funding in international arbitration. On August 31, 2017, the China International Economic and Trade Arbitration Commission Hong Kong Arbitration Center (CIETAC) released its Guidelines on Third Party Funding in Arbitration. These guidelines provide specific principles and practices for parties and arbitrators involved in current or anticipated arbitration procedures managed by CIETAC that include or may include third-party funding.

Emerging Issues

In its recent years of evolution, TPF has encountered various challenges. Currently, the constraining characteristics of relevant legislation (including the delineation of 'party' and 'costs') and the jurisdictional authority wielded by tribunals over third parties (beyond conventional agency and assignment principles) lead to a deficiency in arbitral practice concerning third-party funders. Notably, while most relevant laws stipulate that the award is binding among parties, the English Arbitration Act 1996 also encompassed within the scope of 'party'—individuals asserting rights under or through them. This interpretation could encompass funders. Nevertheless, the courts have consistently construed the term 'party' narrowly only to encompass parties through agency and subrogation doctrines. Unless arbitral practice develops further or relevant laws progress to involve funders in cost decisions explicitly, this authority largely hinges on exercising discretion and applying third-party principles, upholding the fundamental principle of arbitration, namely, party agreement. While examining the origins of consensual dispute resolution is crucial, arbitral practice suggests a broader perspective to include third-party funders in specific scenarios to serve the interests of fairness and justice.

Third-Party Funding in India

At a legal technology innovation conference hosted by Cyril Amarchand Mangaldas, a leading law firm in India, former Supreme Court judge B.N. Srikrishna and another former Chief Justice of the Supreme Court argued that parliamentary legislation is essential for regulating third-party funding. Justice Srikrishna highlighted the challenges of implementing such regulations solely through judicial interpretation of existing legal frameworks. Third-party funding has rapidly grown and is increasingly recognised as a viable and accessible means of financing disputes. The world's largest third-party funder manages an investment portfolio valued at $2.4 billion, with a market capitalisation of approximately $3.2 billion. Although the concept of third-party funding is not new to the Indian legal market—where informal trading of cases has occurred—it remains in its nascent stages of development. Despite outperforming traditional investment options like private equity, real estate, credit, and hedge funds, third-party funding has yet to be established as a recognised asset class in India. This sentiment was echoed by legal professionals in India, with seventy per cent of them expressing the belief that third-party funding is prohibited under current Indian laws.[xlvi]

Historically, India has seen agreements for third-party litigation funding, known as pactum de quota litis, dating back to the 1800s, before the formal codification of contract law. As the Indian legal system aligns with common law traditions, restrictions on champerty and maintenance are believed to be relevant in this context. However, the judicial landscape has been marked by conflicting judgments, resulting in uncertainty regarding the enforceability of such agreements.

The absence of any reference to third-party funding in the Arbitration and Conciliation Act 1996 is significant. Although state-modified Civil Procedure Codes include provisions for third-party funding, this does not automatically extend to arbitration proceedings. Consequently, the validity of any third-party funding arrangement would depend on its compliance with the Indian Contract Act of 1872. Additionally, the logistics of channelling third-party funding in and out of India present unique challenges governed by the Foreign Exchange Management Act of 1999 (FEMA) and its associated regulations. FEMA classifies all transactions involving foreign exchange and non-residents into current and capital account transactions, but it does not categorise third-party funding under either of these. The implications of such funds within the regulatory framework remain uncertain, particularly as these types of transactions are treated quite differently according to FEMA regulations.[xlvii]

In a recent petition for execution filed with the High Court of Hyderabad, the respondents are challenging enforcing an arbitral award issued by Sir Phillip Otton in a London-seated arbitration governed by the International Chamber of Commerce (ICC) rules.[xlviii] One reason for contesting the award is the allegation that the petitioners entered into a third-party funding arrangement, which the respondents claim makes the execution impermissible due to the champertous nature of the funding agreement, thereby violating Indian public policy. While the matter is currently sub judice, the authors believe that based on the Indian legal principles discussed earlier, including the Code of Civil Procedure 1908 provisions, such agreements are not unlawful and can be upheld in India unless they directly contravene established public policy.

Regulatory Framework

Before delving into a potential regulatory framework for overseeing third-party funding in India, initiating a public discourse on the topic involving the general public and relevant interest groups would be prudent. Discussions about third-party funding have largely been limited to the legal community and academia, leaving disputants with a narrow understanding of its significance and benefits. As reliance on arbitration grows in India, questions about the costs associated with funding such proceedings—and the role of third-party funding in alleviating these financial burdens—highlight the need for a transparent and inclusive dialogue. The Law Commission of India, positioned uniquely within the landscape of legislative reform, is well-placed to facilitate a comprehensive public consultation process on third-party funding. Although it is not a constitutional or statutory body, the Commission is an advisory entity established by the Government of India to propose legislative changes. While its recommendations are non-binding, Article 39A of the Directive Principles of State Policy in the Indian Constitution underscores the state's duty to ensure equitable justice for its citizens. As such, the legislative reforms proposed by the Commission are significant, and its reports are highly regarded for their thorough, research-driven approach, often resulting in nuanced suggestions.

Soft law and light-touch approach

One of the matters to be addressed while formulating regulation would involve the decision between implementing a hard or soft law approach towards overseeing third-party funding within the Indian context. Opting for a complicated law approach would entail establishing mandatory regulations applicable to funders and parties engaged in such activities. Nevertheless, given the developing nature of the third-party funding sector and the ongoing evolution of its various dimensions, India should consider adopting a soft law approach instead.

This approach would entail implementing non-binding regulations to guide the behaviour of parties and funders, creating an optimal environment for exploring third-party funding before it gains widespread acceptance in India. As the sector matures, these regulations could provide a framework for formal legislation, should it be deemed necessary.

A prime example of the soft law approach is the Code of Conduct for Litigation Funders (the "Code") issued by the Association of Litigation Funders of England and Wales (ALF). Although the Code primarily focuses on regulating funding in litigation and domestic arbitration within England and Wales, the core principles of third-party funding are also relevant in international commercial arbitration. The ALF Code is a helpful reference for India as it considers the various aspects of third-party financing that may require prompt regulatory attention.

Conclusion

Third-party funding (TPF) is becoming an essential tool in international arbitration. It offers financial backing to claimants who may find it challenging to pursue valid claims due to the high costs associated with arbitration. Although TPF improves access to justice and equalises opportunities, it also introduces several issues, such as potential conflicts of interest, concerns surrounding confidentiality, dominance by funders, and the possibility of baseless claims. The regulatory environment for TPF differs between jurisdictions; for instance, Singapore and Hong Kong have implemented laws to regulate its application, whereas countries like India still lack a detailed framework. The lack of clear regulations in India leads to ambiguity about their applicability, enforceability, and ethical considerations. With India's goal of establishing itself as a global arbitration centre, creating a structured approach to TPF is vital. A well-regulated TPF system can ensure that arbitration remains a reliable and effective method for resolving disputes while promoting economic development and legal certainty by achieving a balance between transparency, fairness, and investor trust. Several issues and considerations have emerged as international commercial and investment arbitration increasingly rely on TPF. While TPF aims to level the financial playing field, thus promoting fairness, it also brings challenges related to disclosure, potential conflicts of interest, and cost implications. These concerns are significant and warrant careful consideration, and any discussions on funding must address these crucial issues while striving to establish a more sustainable and legally sound framework for TPF.

TPF is expected to become a permanent fixture in the landscape of litigation and arbitration rather than being employed temporarily. The legal principles governing its utilisation and the intricate issues that may arise as its usage expands necessitate a well-rounded legislative and judicial approach, both at the domestic and international levels. This approach should consider the apprehensions of industry stakeholders, parties involved, arbitrators, and third parties. Such a comprehensive approach is anticipated to mitigate the current uncertainties and foster the development of robust and widely accepted TPF structures in the foreseeable future.

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