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THE POTENTIAL REGULATION OF THIRD-PARTY FUNDING IN ARBITRATION IN KENYA

WHITE-PAPER REPORT

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PREFACE

I. TERMS OF REFERENCE

Third-Party Funding is on the rise and has become increasingly common in numerous jurisdictions. Third-Party Funding is usually used in situations where a party lacks financial resources to pursue its own claims in arbitration or litigation. The funding agreement regularly provides that the funder will pay costs of arbitration or litigation proceedings for the funded party in return for a percentage of the judgment or award or any other financial benefit from any proceeds recovered by the funded party from the funded proceeding. In case there should be no recovery, the funded party will not have to pay any return to the funder.

Kenya's arbitration practice is on the rise and there is a general policy aim of enabling and improving the alternative dispute resolution mechanisms in the country. A party participating in an arbitration proceeding taking place in Kenya which is considering to seek Third-Party Funding may wish to know if Third-Party Funding is permitted by Kenyan law.

The legal doctrines of maintenance and champerty, developed about 700 years ago in England, have been held by common law jurisdictions, like Kenya, to prohibit Third-Party Funding of litigation both as tort and criminal offence with some exceptions.[1]

It is unclear whether the doctrines of maintenance and champerty also apply to Third-Party Funding for arbitrations taking place in Kenya. To the best of our knowledge, there have not been any public court decisions on that matter in Kenya.

[1] See below, chapter 2.

II. FORMAT OF THIS PAPER

This White-Paper Report was written by the TradeLab Team of Università Bocconi consisting of:

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under the supervision of Professor Catherine Rogers and in close collaboration with Ms Victoria Kigen, case counsel and representative of the NCIA in relation to this project.

The TradeLab Team has met on a regular basis with Professor Rogers and Ms Victoria Kigen to discuss and consider the matters within the Terms of Reference. The recommendations of Chapter 5 of this paper are the result of this group work. They represent the teams' preliminary views, with the purpose for consideration by legislative authorities in Kenya, arbitration practitioners, arbitration service providers and those with an interest in this subject.

We anticipate that this paper will be a solid initial reference point in considering legislative acts to regulate third party funding in Kenya. The main purpose of this report is to serve as a common starting point when developing and discussing ideas, about a potential regulation of Third-Party Funding for arbitral proceedings in Kenya. Preferably, we except this to be done in a working group including governmental representatives and stakeholders of arbitration in Kenya, particularly the NCIA.

In this context, it should be mentioned that the issue of investment arbitration is excluded from our recommendations and only briefly touched upon throughout the report. We believe that the issue of investment arbitration would have gone beyond the scope of what can usefully be

addressed given the purpose of this report. Nevertheless, we think that the basic ideas and concepts of this report can also be of help when considering the issue of investment arbitration.

The White-Paper Report consists of the following chapters:

- Chapter 1 provides background on Third-Party Funding and a general introduction into the topic.
- Chapter 2 provides an overview of the Kenyan legal regime and Third-Party Funding regulations in that concern.
- Chapter 3 examines Third-Party Funding of various other common law jurisdictions.
- Chapter 4 analyses the benefits and risks of Third-Party Funding for arbitration.
- Chapter 5 sets out the recommendations.

III. EXECUTIVE SUMMARY

Chapter 1

Every legal system faces a similar access to justice challenge. Third-Party Funding can be part of the solution to the access to justice issue by aiding the financing of claims that would not have reached the courts because of a lack of resources of the parties involved. There is no single, internationally accepted definition for Third-Party Funding and depending on the chosen literature, contingency fees and After-the-Event Insurance may be included in the definition. In most definitions, three defining concepts must be present: I. non-recourse financing of legal proceedings,[2] II. provided by a party that had no previous ties and interest to the claim III. usually for a

[2] " Non-recourse finance is a form of financing where the lender is only entitled to repayment from the profits of the project, not from other assets of the borrower." Antje Baumann & Michael M. Singh, 'New Forms of Third-Party Funding in International Arbitration: Investing in Case Portfolios and Financing Law Firms' (2019) 7 Indian J Arb L 29

percentage of the monetary outcome of the proceedings if the funded party succeeds.[3] In some states such as the United Kingdom, Third-Party Funding is a generally accepted practice, and it is regulated. However, unified regulation is yet to be set for international and national Third-Party Funding cases.

Chapter 2

The Kenyan Legal Regime is ambiguous in regard of the legality of Third-Party Funding. The several law statutes affecting litigation and arbitration do not explicitly regulate or even mention Third-Party Funding. What has the potential of raising doubts about the legality of Third-Party Funding in Kenya are the doctrines of champerty and maintenance which are still in force in Kenya. The common law principles of maintenance and champerty are generally understood as legal concepts prohibiting third parties with no direct interest in a legal proceeding from funding or profiting a legal proceeding. Originally developed for litigation, they may also be applicable for arbitral proceedings. A strict interpretation could lead to Third-Party Funding agreements to be invalid under Kenyan law which could discourage potential funders from entering the Kenyan market.

Chapter 3

Recent reforms in other common law jurisdictions have been reducing the doctrines of maintenance and champerty to allow Third-Party Funding. Since the legal availability of funding is an important consideration for parties, the availability of Third-Party Funding certainly affects the decision of parties when choosing the seat of arbitration. If this sector is predominantly self-regulated in England, on the other hand Singapore and Hong Kong have recently enacted legal reform to legalize Third-Party Funding using a light-touch approach. Moreover, Nigeria and South Africa

[3] Antje Baumann & Michael M. Singh, 'New Forms of Third-Party Funding in International Arbitration: Investing in Case Portfolios and Financing Law Firms' (2019) 7 Indian J Arb L 29

are actively examining issues relating to Third-Party Funding as a result of the large volume of foreign investments in Africa. In all common law jurisdictions analyzed there is not a general acceptance to leave Third-Party Funding wholly unregulated.

Chapter 4

The Chapter 4 discusses the potential benefits and risks of Third-Party Funding for commercial arbitration. Third-Party Funding is a growing practice and some jurisdictions have decided to clearly permit it. If Kenya decides to clarify the status of Third-Party Funding, an assessment of the benefits and risks of the practice would greatly contribute to the debate in relation to whether it should be permitted.

In this Chapter, the following benefits and risks of permitting Third-Party Funding in arbitration have been identified.

Permitting Third-Party Funding in Kenya would benefit to the parties of arbitration disputes in Kenya by enhancing the efficiency of the mechanism and facilitating the access to justice, especially in the aftermath of the pandemic. It would also benefit to Kenya directly, especially by giving the signal that Kenya is an arbitration-friendly jurisdiction, cognizant of the best modern practices; while prohibitions of Third-Party Funding may deter international parties to choose it as a seat of arbitration.

The use of Third-Party Funding however comes with some concerns. Amongst them, the risk of unnecessary proceedings, the possibility for Third-Party funders to control and influence the case, the questions arising in relation to costs of Third-Party Funding and recoverability, security for costs and liability for adverse costs. Third-Party Funding may also lead to the potential breach of legal professional privilege and confidentiality. Conflicts of interests that may arise with Third-Party Funding are another issue, and nourish the debate surrounding the disclosure of Third-Party Funding agreement. Some potential safeguards addressing these risks are already mentioned in this part.

The question that we propose to keep in mind when discovering this part of the report is whether the benefits of permitting Third-Party Funding outweigh the accompanying risks.

CHAPTER 1

BACKGROUND ON THIRD-PARTY FUNDING

I. INTRODUCTION TO THIRD-PARTY FUNDING

Every legal system faces a similar access to justice challenge: how can they ensure that people who have legal needs are able to afford to pursue or protect those needs. Access to justice is a multidimensional principle expanding to both procedural, and substantive aspects of the justice system in terms of accessibility and it aims to achieve equal access to justice. This principle governs most modern world legal systems, but it is unfortunately hard to apply, raising access to justice issues for citizens. One of the ways in which access to justice can be increased is through legal aid and other forms of funding that enable people to pursue their legal rights even if they lack the resources to do so themselves. Numerous methods for funding litigation and arbitration are used to provide solutions to the access to justice issue and these include Contingency Fees, Insurance and Third-Party Funding.

This report will analyze Third-Party Funding in terms of definition, in the context of arbitration in Kenya and other jurisdictions producing certain conclusions and specific recommendations for Third-Party Funding in Kenya's legal system.

(a) Managing the costs of litigation and arbitration

Third-Party Funding can be part of the solution to the access to justice issue by aiding the financing of claims that would not have reached the courts because of a lack of resources of the parties involved.

Various parties can benefit from Third-Party Funding, the first being natural persons who are either claimants or defendants involved in disputes.[4] In addition, companies involved in legal proceedings can also benefit from Third-Party Funding. Insolvent or small companies that do not have readily available funds to pursue claims and larger companies that often face constant lawsuits can have access to funding and cash flow to pursue claims and fund their legal proceedings while decreasing the risks associated with negative legal outcomes.[5]

Third-Party Funding can therefore offer many benefits to the traditional issue of access to justice by securing funding for parties to the disputes, from natural persons to smaller and large companies, both claimants and respondents.[6]

(b) Sources of Funding in Litigation and Arbitration

The access to justice issue is complex and does not have a single right solution. Several options are however available for parties facing this issue. Third-Party Funding is one option among a range of options that can be used to finance the cost of disputes. Many of these have been around for much longer and are therefore more widely regulated. Contingency Fees and Insurance Agreements as options to the access to justice issue will be analyzed below.

1. Contingency Fees

Contingency fee agreements are one of the options that are available for the funding of disputes.

Under contingency fee arrangements, legal counsel is not paid their regular fees but instead their fee is dependent on the outcome of the case. These

[4] Victoria Shannon Sahani, Judging Third-Party Funding, 63 UCLA L. Rev. 388 (2016)
[5] Ibid
[6] Ibid

agreements cover a variety of result-based fees claimed by lawyers as payment for their legal services.[7]

Fees are generated depending on the negative or positive outcome of the case.[8] In the cases where the outcome of a dispute is negative, counsel may either not receive a fee or receive a fee that is typically greatly reduced compared to the usual fee paid to counsel in the absence of a contingency fee arrangement.[9] In the cases where the outcome of the dispute is positive, counsel is either entitled to a percentage of the reward or is paid the standard fee oftentimes including an "uplift" to that.[10]

Despite their popularity in some counties like the United Kingdom and the United States, contingency fees are nevertheless controversial in other jurisdictions.

In Europe, the debate over the risks and benefits of contingency fees can be summarized in the following: One of the risks arises from the ethical obligation of lawyers who are under a duty to defend their client and to defend justice. Personal investment in the monetary outcome of the case may raise conflicts of interest ethically and in practice. Specifically, it is feared that lawyers may pursue personal gain breaching the duty owed to their client and the justice system. It flows from this argument that the personal investment of lawyers in the claim may harm the client-lawyer relationship. Clients may have doubts about whether or not their lawyer has their best interest in mind or whether their lawyer is pursuing personal gain from the case. Contingency fee arrangements that have negative outcomes could even drive lawyers to engage in questionable practices in order to compensate for their loss, although this argument is not entirely convincing,

[7] Mark Tuil, Louis Visscher, "New Trends in Financing Civil Litigation in Europe: A legal, empirical and economic analysis", Edward Elgar Publishing Limited [2010]
[8]Eric Helland & Alexander Tabarrok, 'Contingency Fees, Settlement Delay, and Low-Quality Litigation: Empirical Evidence from Two Datasets' (2003) 19 J L Econ & Org 517
[9] Contingency Fees Act 66 of 1997
[10] Mark Tuil, Louis Visscher, "New Trends in Financing Civil Litigation in Europe: A legal, empirical and economic analysis", Edward Elgar Publishing Limited [2010]

and it questions the ethics of the legal profession collectively. It is also argued that access to justice is not enabled through such agreements because weaker claims will not be pursued, or cases with no merit may be taken on too easily.

In the United States, Contingency Fees are widely used often advertised under the "no win, no fee" campaign.[11] Despite their popularity, even in the United States some critics contend that the ability to bring cases on a contingency fee basis can increase the number of cases brought without a high probability of success. In other words, the concern is that the availability of contingency fees may increase the number of frivolous cases.[12] Clients and lawyers may pursue claims in the hopes of gaining a settlement without any expectation that they will actually have to reach a trial phase to prove the merits of a case in a trial.[8]

Contingency fees are therefore controversial and while they can aid access to justice for some parties, they may increase frivolous claims and create conflicts of interest between clients and their lawyers.

2. Insurance

Insurance is another resource that can enable parties to finance their litigation and arbitration proceedings. There are several types of insurance agreements that may provide funding for a claim.[13]

i. Liability Insurance

Liability Insurance is the most common types of insurance that covers litigation and arbitration costs. Traditionally when a party has liability insurance and is subsequently sued, the insurance company funds and

[11] Eric Helland & Alexander Tabarrok, 'Contingency Fees, Settlement Delay, and Low-Quality Litigation: Empirical Evidence from Two Datasets' (2003) 19 J L Econ & Org 517
[12] David McQuoid-Mason, "Access to Justice in South Africa:Are there Enough Lawyers?"[2013] Onati Socio-Legal Series, Vol. 3, No. 3
[13] Lisa Bench Nieuwveld, Victoria Shannon Sahani, Third Party Funding in International Arbitration (First Pulished 2012, Wolters Kluwer)

defends the client against proceedings, possible awards and damages or judgments. Liability insurance is commonly used in malpractice and automobile claims where disputes arise often but they remain minor and can be settled promptly.[14] Under most insurance contracts, the insurance company undertakes a big part of the responsibility of the case if not sole responsibility, having the power to assess each case and decide whether to pursue it or settle it. Choice of counsel is often also decided by the insurance companies.[15]

Liability insurance is therefore one of the most commonly used types of insurance, covering the fees of litigation and arbitration, depending on the contract terms and is undertaken before the occurrence of the event giving rise to the dispute. This type of insurance usually gives significant control of the insurance company over the process and pursuit of the claim.

ii. Before-the-Event and After-the-Event Insurance

Distinct from liability insurance, certain types of insurance agreements can provide coverage for a significant part of litigation costs while also giving up less control to the insurance company over the case management.[11] These types of insurance include Before-the-Event Insurance and After-the-Event Insurance.

Before the Event Insurance is purchased before the event that gives rise to the legal proceedings occurs. It is designed to cover the costs of litigation of the insured client. In those jurisdictions in which a winning party may also be awarded reimbursement of their litigation costs, Before-the-Event Insurance can also cover the costs of reimbursing the wining party.[12] Before the Event insurers are usually not as involved in case management as Third-Party Funders are. Evaluation of the cases is also an element that is absent

[14] Lisa Bench Nieuwveld, Victoria Shannon Sahani, Third Party Funding in International Arbitration (First Pulished 2012, Wolters Kluwer)
[15] Lisa Bench Nieuwveld, Victoria Shannon Sahani, Third Party Funding in International Arbitration (First Pulished 2012, Wolters Kluwer)

from Before-the-Event Insurance procedures and that is because the insurance is purchased before the need for litigation/arbitration arises.[16]

After-the-Event insurance is agreed upon after the event giving rise to the legal proceedings occurs. After-the-Event Insurance provides coverage for costs incurred by a party when his case is unsuccessful. This could include adverse costs owed to the winning party and their own costs, often, but not always including counsel fees. The coverage of After-the-Event Insurance depends on the type of claim pursued by the party and it can therefore cover more or less legal proceedings costs depending on the merits of the case and success probability.[17]

Similarly to Third-Party Funders, After-the-Event insurers usually evaluate the cases brought to them and monitor the case more closely. In practice, when a party is exploring insurance options to fund a claim, usually Before-the-Event insurance would be the first option since it traditionally provides more extensive coverage of legal fees than after the event insurance. Where Before-the-Event insurance is not possible, After-the-Event insurance can be pursued and it can also be paired with a contingency fee agreement.[18]

Following this analysis, although Before and After-the-Event insurance are not substitutes to legal aid, they can increase access to justice by offering a chance to claimants to pursue their claims. Due to the similarities of After-the-Event insurance and Third-Party Funding, after the event insurance is defined as a form of Third-Party Funding.

II. THIRD-PARTY FUNDING: DEFINITION AND TYPES

(a) Defining Third-Party Funding

[16] Richard Nash, "Financing Access to Justice: Innovating Possibilities to Promote Access for All" [2013] 5: 96-118
[17] Jackson Report
[18] Lisa Bench Nieuwveld, Victoria Shannon Sahani, Third Party Funding in International Arbitration (First Pulished 2012, Wolters Kluwer)

There is no single, internationally accepted definition for Third-Party Funding. Instead, Third-Party Funding is an overarching term that can include many forms of Third-Party Funding. As mentioned previously in this paper, some funding options such as After-The-Event Insurance can either be included or excluded from the Third-Party Funding definition depending on the available and preferred literature. Nevertheless, a basic definition is helpful as a basis for examining how Third-Party Funding works.

Third-Party Funding is the funding of a dispute by any person or entity that is not party to the dispute, for a fare dependent on the success and monetary gain from the outcome of the dispute, as decided upon and negotiated by the funder and the funded party.

More specifically, Third-Party Funding usually includes three concepts:

I. non-recourse financing of legal proceedings,[19]

II. provided by a party that had no previous ties and interest to the claim

III. usually for a percentage of the monetary outcome of the proceedings if the funded party succeeds.[20]

In order to make the definition clearer, it is essential to analyze each term and concept of Third-Party Funding in detail.

For the purposes of the definition, the funded party can be any individual or legal entity that is party to a dispute or claim following the track of litigation or arbitration at a national or international level. As mentioned in the introduction, this can include claimants and defendants that can be natural or legal persons or companies involved in legal proceedings. Companies that can receive funding for their legal proceedings can be

[19] ” Non-recourse finance is a form of financing where the lender is only entitled to repayment from the profits of the project, not from other assets of the borrower.” Antje Baumann & Michael M. Singh, 'New Forms of Third-Party Funding in International Arbitration: Investing in Case Portfolios and Financing Law Firms' (2019) 7 Indian J Arb L 29

[20] Antje Baumann & Michael M. Singh, 'New Forms of Third-Party Funding in International Arbitration: Investing in Case Portfolios and Financing Law Firms' (2019) 7 Indian J Arb L 29

insolvent, small or larger companies that either have limited resources available for legal costs or often face constant lawsuits and limited cash flow to support their claims.[3]

The Third-Party Funder can be any person or entity providing the funds for the legal costs of the parties to the dispute. The funder can take the form of a bank, insurance company, hedge fund or any entity that provides the funding. The funder is not a party to the dispute and has no ties to the dispute other than the agreement made with either the defendant or claimant. Essentially, the Third-Party Funder is in no way involved in the dispute and the only ties are created between the funder and the dispute are through the agreement of the Third-Party Funder and the funded party while the funder remains a non-party to the dispute.

Non-recourse funding limits the profits of the funder to an agreed upon part of the profits gained from the outcome of the funded claim. It is therefore a characteristic of Third-Party Funding that protects the funded party from being personally liable with their assets to the funder.

The funder recovers a percentage of the award or judgment outcome of the claim and the calculation of this will be based on the merits and risks associated to the case. The percentage of recovery for the funder is also a result of the negotiations between the funder and the funded party.

(a) How is Third-Party Funding Acquired

Third-Party Funding will usually be established through a contract that will be the result of negotiations between the funded party and the Third-Party Funder.

That said, the contract must at least regulate the nature and specific terms of the agreement. Specifically, the funder will usually seek as a product from the Third-Party Funding arrangement, a percentage of the final reward

in the case of a successful result to the dispute. The product can however take several forms.[21]

The percentage of return for the funder might often be based on the amount of risk associated with the success or failure of the case. During the selection process of potential cases that may be funded, a Third-Party Funder will conduct a screening process, assessing the merits of the claim, the type of claim, the chances of success and other factors that would affect the possibility of returning a product from the Third-Party Funding to the funder. It is essential to note at this point that during a Third-Party Funding agreement and especially when the agreement is made in a common law jurisdiction that is still governed by the doctrines of maintenance and champerty, it is very important for the parties to the agreement to consider the ”control rights” of the funder.

(b) The forms of Third-Party Funding

Third-Party Funding can take many different forms. The legality of each one depends on the legislation and regulations of each legal system. In the legal systems that allow Third-Party Funding, there are various ways a Third-Part Funding arrangement can be organized.

Apart from the traditional model of Third-Party Funding Contingency Fees and After-the-Event Insurance, Defense-side Funding and Investment will be briefly analyzed below as forms of Third-Party Funding.[22]

1. Contingency fees and Insurance in the context of Third-Party Funding

[21] (i) the return generated by multiplying funded costs by a pre-designated multiplier (often based upon a three-to-one ratio), or (ii) a percentage interest in any recovery achieved (often in the range of 20 per cent to 40 per cent of amounts recovered)." Funders may also set a minimum guaranteed return, set as a function of the amount invested by the funder.

[22] The Law Reform Commission of Hong Kong, *Third Party Funding for Arbitration* (Report, 2016) Ch3

As analyzed above, under some definitions of Third-Party Funding contingency fees may be considered a form of Third-Party Funding. Traditionally, Third-Party Funding is usually defined as including an investment of "third-party capital".[23] In the case of contingency fee arrangements a non-party to the dispute, covers the costs of the legal proceedings and the risk of loss arising from the potential unsuccessful outcome of the proceedings is assigned to the third-party, in this case the lawyer or law firm.[24]

In Third-Party Funding agreements, the Third-Party Funder invests capital, and the choice of counsel is not "locked" by definition as it is in contingency fee arrangements. The investment is therefore monetary.[23] Contingency Fee arrangements lack the concept of "third-party capital" investment. The investment is instead in the form of labor put into the preparation of the case. Because of that fundamental difference, contingency fees are usually not considered to be a form of Third-Party Funding. Third-Party Funding Agreements in their default form can however, be combined with contingency fee arrangements. However, such agreements are sometimes disliked by third-party investors since their presence may increase the involvement of counsel in the investment outcome or it can even make counsel co-investors.[24]

Similarly to contingency fee arrangements, the definition of Third-Party Funding can also encompass certain types of litigation insurance contracts where the insurer covers the costs of litigation. Specifically, because of the similarities of After-the-Event Insurance to Third-Party Funding, this type of insurance is often considered to be a type of Third-Party Funding. This approach is followed by the ICCA Queen Mary report on Third-Party Funding.[25] However, in relevant literature, it is argued that the nature of

[23] Maxi Scherer & Aren Goldsmith, 'Third Party Funding in International Arbitration in Europe: Part 1 - Funders' Perspectives' (2012) 2012 Int'l Bus LJ 207
[24] Maxi Scherer & Aren Goldsmith, 'Third Party Funding in International Arbitration in Europe: Part 1 - Funders' Perspectives' (2012) 2012 Int'l Bus LJ 207
[25] Report of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration, International Council for Commercial Arbitration, April 2018

insurance is different than the nature and purpose of Third-Party Funding. Namely, insurance is used to minimize the adverse costs that may arise from disputes whereas Third-Party Funding is a funding option for disputes. The equation of these two options is therefore still being debated. For the purposes of this paper, following the Queen Mary approach, after the event insurance will be analysed as a form of Third-Party Funding.

2. Defendant/respondent-side funding

Although most Third-Party Funding focuses on funding the Claimant, Third-Party Funding is in theory available for responding or defending parties under certain circumstances.

In this kind of arrangement, a defendant may seek for the funding for a counterclaim. In this situation, the Third-Party Funding arrangement is analogous to claimant-side funding.[26]

Reverse contingency fees can also be used to fund a defendant's claim. In such cases the funder's recovery will be calculated considering the amount that was saved by the defendant as opposed to the original amount of compensation claimed by the claimant. The amount saved will then be multiplied in accordance with the Third-Party Agreement terms regarding the funder's recovery.[27]

There are several other situations under which defendant/respondent-side funding may be available but in practice, it is not a phenomenon that often arises in Third-Party Funding.[28]

3. Investment Third-Party Funding

[26] Bernardo M. Cremades, Jr,"THIRD PARTY LITIGATION FUNDING: INVESTING IN ARBITRATION"[2011]
[27] Aren Goldsmith & Lorenzo Melchionda, 'Third Party Funding in International Arbitration: Everything You Ever Wanted to Know (but Were Afraid to Ask)' (2012) 2012 Int'l Bus LJ 53
[28] Ibid

Third-Party Funding has also recently been pursued as an alternative form of investment departing from the traditional investment options such as investing in the stock market.[29] Investment Third-Party Funding is increasingly popular in international arbitration and litigation. In Investment Third-Party Funding, a Third-Party Funder, usually invests in a "portfolio" of cases. Some Third-Party Funders even invest in law firms as "portfolio investments", providing funding for the law firm that uses the funds to take on cases with high chances of success. In such cases, the law firm will take on the cases on a contingency fee basis.[30] This is however a topic in need of further analysis and won't be the focus of this paper.

(c) Structure and Terms in a Third-Party Funding Agreement

Third-Party Funding is established through a funding agreement. The structure and terms of a Third-Party Funding Agreement are negotiated between the Third-Party Funder and the funded party. However, there are several crucial topics that are typically addressed in Third-Party Funding Agreements. The specific provisions may differ among different funders and disputes. However, a number of terms in Third-Party Agreement are relatively standard. These terms include:

i) The payment of lawyers' fees and litigation costs by the Funder, which includes an exact calculation of the funder's compensation and the circumstances under which the payment shall occur must be specified.[31]
ii) The order of payment of such compensation in the case of a successful claim[32]

[29] Antje Baumann & Michael M. Singh, 'New Forms of Third-Party Funding in International Arbitration: Investing in Case Portfolios and Financing Law Firms' (2019) 7 Indian J Arb L 29
[30] Ibid
[31] Antje Baumann & Michael M. Singh, 'New Forms of Third-Party Funding in International Arbitration: Investing in Case Portfolios and Financing Law Firms' (2019) 7 Indian J Arb L 29
[32] Ibid

iii) The Funder's liability for costs- including adverse costs and Security for costs[33]

iv) The conditions under which a funder may terminate or withdraw funding[34]

v) The extent of a Funder's control and management over the proceedings[35]

vi) The method of resolution of disputes between the funder and funded party. Specifically, a Third-Party Funding Agreement may include a dispute resolution clause for the funding agreement itself[36]

vii) The funder and funded-parties confidentiality obligations[37]

These provisions are described in greater detail below.

1. Control over the conduct of proceedings

In the agreement, the amount of control that the funder can have over the legal proceedings must be specified. This arrangement is important because often disputes may arise between the funder and funded party or even the legal counsel regarding the way to proceed with the case. It is also important to specify the amount of control because depending on the jurisdiction under which the agreement has been concluded, argued abuse of power by the funder may deem a Third-Party Agreement unenforceable.

In common law jurisdictions where the principles of maintenance and champerty are present, if the amount of control of the funder is considered to be excessive, the Third-Party Funding agreement could be deemed unenforceable in the courts. These principles and their effects will be further analyzed in the following chapters of the report. In the England and Wales Third-Party Funding Code it is stated that pressure to give up control to the Funder will not be tolerated. In the agreement therefore it is important to

[33] Ibid
[34] Ibid
[35] Ibid
[36] Ibid
[37] Ibid

specify the amount of control that will be given to the funder, the legal team and the parties to the dispute in order to avoid direct conflicts regarding control and indirect conflicts such as strategic disagreements that might come up.

The Funder's control over the proceedings is a significant provision in a Third-Party Funding Agreement firstly because regulating the relationship between the funder, the case and the involved parties, will minimize disputes that may arise between them, and secondly because in certain jurisdictions abuse of control by the funder can deem the agreement unenforceable.

2. Conflicts of Interest

It is vital to consider potential conflicts of interest between the attorneys, Third-Party Funder and the funded party. The American Bar Association Commission on Ethics has issued a report on good practice tactics for lawyers when Third-Party Funding Agreements are in place. The most significant conflict of interest appears to be when the said conflict affects the relationship between the client and attorney.

3. Termination and withdrawal of funding

In the agreement, it is useful to include the terms under which funding may be withdrawn. This situation can often occur when it is deemed by the funder or counsel that the claim is no longer viable or has lost its chances of success over time because of a change of circumstances. Termination may also occur where there has been a breach of the terms of the agreement in question. In this part of the agreement, dispute resolution clauses may also be introduced to cover potential disputes arising from the termination or consideration for termination of the agreement.[38]

[38] The Law Reform Commission of Hong Kong, *Third Party Funding for Arbitration* (Report, 2016) Ch3

4. Liability for costs, including Adverse Costs Orders and Security for Costs

Parties and funders usually specify in a Third-Party Funding Agreement whether the Third-Party Funder will be liable for adverse costs order and security for costs. This means that it might be agreed upon that the funder will bear the legal costs of the opposing party in the case of an unsuccessful claim.[39]

Alternatively, the party may separately purchase After-the-Event Insurance to cover the said costs. It is therefore possible when liability for costs is not covered by the Third-Party Funding agreement, that a party takes on both After-the-Event Insurance and a Third-Party Funding Agreement in order to acquire more coverage of the legal costs incurred.[40]

5. Attorney-client privilege, Party conflict management and dispute resolution

When a Third-Party Agreement is in place, the Third-Party Funder, -depending on the agreed control that he may have over the legal proceedings as discussed above in section II.a.- may request information regarding the claim that would otherwise be protected under the attorney-client privilege and would thus not be disclosed with any third-parties. The issue raised is that privileged information that is disclosed with third-parties deems attorney-client privilege of that information waived. The confidentiality standards between a Third-Party Funder and the funded party are weaker and lower than the confidentiality standards between the attorney and his client-the funded-party and client being the same entity. This raises several issues regarding conflicts of interest that may arise between the funder and other cases that he is funding because of possible disclosure of privileged information from the funder.

[39] Aren Goldsmith & Lorenzo Melchionda, 'Third Party Funding in International Arbitration: Everything You Ever Wanted to Know (but Were Afraid to Ask)' (2012) 2012 Int'l Bus LJ 53

[40] Ibid

Despite the importance of this issue, most regulations and regulating bodies for Third-Party Funding have left this topic undiscussed. The most common approach in national and international arbitration is to leave the consideration of this issue to at the discretion of the arbitrator.

The most prominent distinction is made between common and civil law countries.

There are some civil law jurisdictions that might extend professional secrecy that attorneys are bound by to Third-Party Funders. Professional secrecy gives the right and professional duty to not disclose any confidential information even if that information is requested by an official authority. This approach is most common in civil law jurisdictions although there have been cases in the United States where confidential funding documents were requested for reveal in the courts.

In common law jurisdictions, especially when a contract is in place, privileged information shall be protected, subject to the agreement terms. However, in most common law jurisdictions, Third-Party Funding is prohibited or not regulated.

III. THIRD-PARTY FUNDING: REGULATION APPROACHES

In some states, Third-Party Funding is a generally accepted practice and it is regulated. For example, in the United Kingdom, the Association of Litigation Funders which is a private organization has been authorized by the national government to draft the code of conduct for Third-Party Funding in collaboration with the Civil Justice Council. The Association can impose sanctions on non-complying Third-Party Funders under the authority that it has been granted by the council. Only members of the Association are governed by the code of conduct and the said membership is voluntary and only addressing commercial rather than consumer Third-

Party Funding.[41] Parties seeking for Third-Party Funding can therefore greatly benefit from collaborating with funders who are members of the Association.

The American Legal Finance Association has also produced a similar code of conduct recognized as legitimate by the government and operating on a voluntary basis only regarding consumer Third-Party Funding.

The International Legal Finance Association operates in the commercial financial funding industry internationally. Apart from a best-practices list, the International Association does not provide information on sanctions, allowing self-regulation for funders.

Further, Third-Party Funding can also be indirectly regulated through regulation of lawyers' conduct in the context of a Third-Party Funding agreement. For instance, the American Bar Association has submitted a report on "Alternative Litigation Finance" which includes a code of conduct for lawyers when taking on cases associated with Third-Party Funding. Although not directly regulating Third-Party Funders' conduct, several lawyers' conducts regulated under the report, including withdrawal from the case if a funder's control is interfering with the lawyers' ability to carry out their professional responsibilities, could significantly affect a funder's conduct with respect to the amount of control they can have over the counsel in a case.

The resemblance of Third-Party Funding, to other forms of investment (e.g. venture capital) often leads to regulation of the financial market also affecting and indirectly regulating Third-Party Funding. In Australia, Third-Party Funders are required to obtain an Australian Financial Services License while the Australian Securities and Investments Commission

[41] Aren Goldsmith & Lorenzo Melchionda, 'Third Party Funding in International Arbitration: Everything You Ever Wanted to Know (but Were Afraid to Ask)' (2012) 2012 Int'l Bus LJ 53

oversees Third-Party Funding adopting a "light touch" approach to its regulation.

Lastly and more importantly, governments have slowly started regulating Third-Party Funding with the prominent example of the Hong Kong "Code of Practice for Third-Party Funding on Arbitration" following the legalization of Third-Party Funding in Hong Kong.

Non-governmental regulations of Third-Party Funding have also produced codes of conduct for international arbitration. For example, the International Council for Commercial Arbitration and the Queen Mary University School of law produced a report with policy suggestions addressing Third-Party Funding extending to international arbitration.

The no regulation approach is however the most common approach worldwide at the moment. The presence of Third-Party Funding and its legality is more often than not, not addressed by governments, with a large number of governments also deeming Third-Party Funding as illegal.

CHAPTER 2

THE KENYAN LEGAL REGIME AND THIRD-PARTY FUNDING

I. INTRODUCTION

The existence and use of Third-Party Funding is dependent on the legal framework of the jurisdiction where the funding is being used. Most prominently, in common law states like Kenya, the doctrines of maintenance and champerty raise doubts about the legality of Third-Party Funding in international arbitration which can potentially scare of Third-Party Funders from entering a certain market. This is especially reasoned on the effects potential legal obstacles could have on the procedural aspects concerning the enforceability of an award but also of the funding agreement itself. The following analysis of litigation and arbitration under the Kenyan legal regime and the legal profession provides background for assessing the legality of TPF in Kenya. This analysis cannot claim completeness, since it is written from a foreign lawyer's perspective, and is therefore intended to give an overview using publicly available information.

II. LITIGATION AND ARBITRATION IN KENYA

Disputes in civil and commercial matters in Kenya are usually resolved by either litigation or arbitration. This chapter provides an overview of the two procedures to highlight aspects that may be relevant if Kenya were to attempt to regulate Third-Party Funding.

(a) Litigation law in Kenya

Litigation is the main method of dispute resolution in Kenya. Kenya's legal system is largely adversarial and as such courts play a passive role over

litigation. However, the court has the power to compel compliance with civil procedure and wide discretion in the conduct and management of litigation proceedings.[42] Furthermore, court proceedings in Kenya are generally public except for certain cases where the court can rule to exclude the public from attending hearings for lawful reasons.[43]

Alternative dispute resolution methods are gaining popularity in Kenya. This trend can largely be explained with the Constitution and the Civil Procedure Act encouraging the use of alternative dispute resolution methods in resolving disputes. In line with Article 159 of the Constitution, the Judiciary established court-annexed mediation (**CAM**) in 2016. Once a case is filed in court, a trained screening officer, usually the Deputy Registrar, assesses the file to determine whether it is appropriate for mediation before proceedings with litigation. Currently, CAM is applied to cases filed in the Commercial and Family Divisions of the High Court. Besides the court-annexed mediation, arbitration is commonly used as a method of alternative dispute resolution in Kenya.

(b) Sources of arbitration law in Kenya

Arbitration is the process by which parties agree to submit any future dispute (or any dispute that has already arisen) to an arbitral tribunal to adjudicate over the dispute resulting from a legal relationship between the parties. Arbitration is most used for (international) commercial disputes and foreign investment disputes through investment arbitration.[44]

Due to an influx of foreign investments in recent years, the selection of arbitration as mechanism for resolving commercial disputes, particularly

[42] Nikhil Desai/Elizabeth Muthoka, *Litigation and enforcement in Kenya: overview* (2021) <https://uk.practicallaw.thomsonreuters.com/w-017-2955?transitionType=Default&contextData=(sc.Default)&firstPage=true#co_anchor_a940893>.

[43] *Ibid*

[44] Nikhil Desai/Elizabeth Kageni, *Arbitration procedures and practice in Kenya* (2021) <https://uk.practicallaw.thomsonreuters.com/5-633-8955?transitionType=Default&contextData=(sc.Default)&firstPage=true>.

involving foreign investors, has increased in Kenya.[45] The natural correlation of a rise in arbitration with the rise of foreign investments can be explained with the demand of foreign investors to rather refer potential cases to arbitral proceeding where they can influence several factors of the proceeding (see below point (e)) than to be handed over to a foreign (procedural) law system in which the investors usually are not familiar with.

The rise of arbitration can be evidenced by the laws (and their reforms) and institutions that have been set up for arbitration proceedings. These new sources include the Arbitration Act which was passed in 1996 and amended in 2009 (the **Arbitration Act**). The Arbitration Act was originally modelled on the UNCITRAL Model Law on International Commercial Arbitration 1985 (**UNCITRAL Model Law**).[46]

In addition to these legislative developments, Constitution of Kenya 2010 (the **Constitution**) also provides specific references to arbitration. It mandates courts and tribunals to be guided by the principles of alternative forms of dispute resolution, including arbitration.[47]

In addition to laws specifically addressing to arbitral process, the Nairobi Centre for International Arbitration Act 2013 (**NCIA ACT**) established the Nairobi Centre for International Arbitration (**NCIA**) and also a set of arbitral rules and which are executed by the NCIA.[48]

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[45] Nikhil Desai/Elizabeth Kageni, *Arbitration procedures and practice in Kenya* (2021) <https://uk.practicallaw.thomsonreuters.com/5-633-8955?transitionType=Default&contextData=(sc.Default)&firstPage=true>.

[46] The United Nations Commission on International Trade Law (**UNCITRAL**) is the core legal body of the United Nations system in the field of international trade law. A legal body with universal membership specializing in commercial law reform worldwide for over 50 years, UNCITRAL's business is the modernization and harmonization of rules on international business. The Model Law is designed to assist States in reforming and modernizing their laws on arbitral procedure so as to take into account the particular features and needs of international commercial arbitration.

[47] John Ohaga/Isaac Kiche, *International Arbitration in Kenya* (2021) <https://iclg.com/practice-areas/international-arbitration-laws-and-regulations/kenya>.

[48] Fuhter information can be found in II(b)2.

Another important legal development that demonstrates Kenya's intention and commitment to provide a stable legal environment for arbitration is its ratification and incorporation of to the Convention on the Recognition and Enforcement of Foreign Arbitral Award 1958 (**New York Convention**). The New York Convention has been incorporated into the Arbitration Act for the recognition and enforcement of international arbitral awards.[49]

1. The rise of arbitration in Kenya and Africa

Due to the confidential nature of commercial disputes, the statistics and details of cases in which Kenyan parties have been involved or where the forum has been provided in Kenya are difficult to ascertain. However, companies prefer arbitration as their dispute resolution mechanism as opposed to the court system.[50]

In the field of investment arbitration, in 2015 Kenya faced two new International Centre for Settlement of Investment Disputes (**ICSID**) cases against it involving natural resources. The cases, filed by investors against the Kenyan government, are *Cortec Mining Kenya Limited, Cortec (Pty) Limited and Stirling Capital Limited v Republic of Kenya and Walam Energy Inc. v Republic of Kenya*. The ICSID Tribunal in the Cortec Mining case in October 2018 issued an award in favour of the Republic of Kenya.

The rise of arbitration in Kenya is part of a larger story of arbitration gaining traction throughout Africa. Founding of the NCIA in 2013 is in keeping with founding of numerous arbitral institutions across Africa in recent years. Currently, nearly 100 arbitration institutions of various sizes and areas of

[49] The New York Convention is an international treaty with 169 parties enabling the effective recognition and enforcement of arbitration awards made in another contracting state by forcing member state courts to recognize and enforce arbitral awards made in other member states.

[50] *Ibid.;* According to the ICC Dispute Resolution Report 2020, Kenya was also chosen for two ICC Arbitration cases as place of arbitration <https://nyiac.org/wp-content/uploads/2021/09/ICC-Dispute-Resolution-2020-Statistics.pdf>, 16.

focus exist across Africa.[51] The top five arbitral centers as chosen by the respondents in Africa are the Arbitration Foundation of Southern Africa (**AFSA**), the Cairo Regional Centre for International Commercial Arbitration (**CRCICA**), the Kigali International Arbitration Centre (**KIAC**), the Lagos Court of Arbitration (**LCA**), and the NCIA.[52]

In addition to arbitral institutions that administer arbitrations, several other entities have been formed to promote arbitration in Africa. For example, in June 2018, African arbitration practitioners launched the African Arbitration Association (**AfAA**) in Cote d'Ivoire which aims to promote and advance the use of international arbitration in Africa. Many young practitioners have developed skills, including obtaining foreign Masters' degrees that enable them to participate in international arbitration practices and thereby contribute to the rise of arbitration in Africa.

Together, all these innovations and sources to facilitate arbitration in Africa underscore the importance and value of NCIA in development of arbitration in Kenya.

2. The Nairobi Centre for International Arbitration

The NCIA is aiming for the promotion of international commercial arbitration and alternative forms of dispute resolution. It offers a neutral venue for administering and executing international arbitration procedures. Furthermore, it administers arbitration proceedings by providing clear procedural guidelines and a case counsel to assist the tribunal in the collation of documents and assist parties in complying with the tribunal directions.

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[51] Wheal/Oger-Gross/Obamuroh/Llonge, *Institutional arbitration in Africa: Opportunities and challenges* (17 September 2020) <https://www.whitecase.com/publications/insight/africa-focus-autumn-2020/institutional-arbitration-opportunities-challenges>.

[52] Emilia Onyema, *2020 Arbitration in Africa Survey Report – Top African Arbitral Centres and Seats* (30 June 2020) 5.

In 2019/2020, seven new disputes were referred to the NCIA all of which were referred under the NCIA Arbitration Rules. Additionally, the NCIA has provided administrative services for ad-hoc arbitrations and acted as appointing authority in five cases. The centre is thereby steadily approaching its 40th case. The case value has significantly risen to Kenya Shillings (**KES**) Seven billion (Kes. 7,086,541,211.40) equivalent to USD 70,865,412.11. This represents a 183.46% growth from the previous year. The agreements anticipated under the NCIA Arbitration Rules are typically commercial disputes. Regarding industry sectors, NCIA Arbitrations commonly relate to construction, supplies and delivery agreements, service agreements and employment disputes. This fact evidences the raising cross-sectoral importance of the NCIA especially for commercial disputes.[53]

Besides its traditional tasks as an arbitration center, it also takes a general policy influencing role with the aim of promotion alternative dispute resolution methods. Further, section 5 of NCIA Act mandates the centre to provide training and accreditation programs for mediators and arbitrators and to educate the public on alternative dispute resolution mechanisms. In the execution of this mandate, NCIA offers accredited training programs for both mediation and arbitration geared toward the promotion of alternative dispute resolution.[54]

Since the NCIA and the NCIA Rules were established, there is a trend of including dispute resolution clauses in government contracts with the NCIA Rules being designated as the applicable rules.[55]

(c) Costs of arbitration

For all its benefits, international arbitration proceedings can be expensive. Like litigation, parties must pay their counsel. But, unlike modest court fees,

[53] NCIA Annual Casework Report 2019/2020
[54] Homepage NCIA, Training & Accreditation <https://ncia.or.ke/training-accreditation/>.
[55] John Ohaga/Isaac Kiche, *International Arbitration in Kenya* (2021) <https://iclg.com/practice-areas/international-arbitration-laws-and-regulations/kenya>.

arbitral fees tend to be higher. In addition, commercial arbitration also often requires significant resources. The amount of the costs varies depending on the circumstances of every individual case and may be influenced by the following features the case:

- the amount in dispute;
- the fees of the legal advisors instructed by the party;
- the length of the procedural timetable set by the Tribunal;
- the complexity and number of legal and factual issues in dispute, the requirement of experts;
- the fees of the Tribunal (varying either due to the set of fees charged by each arbitral institution or the fees of each arbitrator as agreed to be paid by the parties);
- the administrative and registration fees of an arbitral institution in cases of institutional arbitration;
- the amount of documentation to be reviewed;
- the costs of holding a hearing (cost of facilities, accommodation and transport for the Tribunal and counsel),
- the costs of enforcing an Award, or applying to a court to challenge or set aside the Award.

The abovementioned costs again can differ between domestic and international arbitration.

For domestic arbitration proceedings administered by the NCIA, there are fixed fees. First, there is a non-refundable registration fee payable to the Centre at the time of filing the request with a maximum of KES 10,000. This amount must be paid by the party initiating the proceeding at commencement of the proceedings. In addition to the registration fee, the NCIA charges an administrative feed in the amount of 1.5% of the rate charged for arbitrator's fees. With respect to arbitrators' fees, each

arbitrator is compensated at an hourly rate of a maximum KES 25,000 per hour. [56]

For international arbitration, the costs are higher. The total fees (including both arbitrator fees and administrative costs) of the NCIA depend on the amount in dispute. For disputes involving amount over 50,000,001 USD, the arbitrator's fee consists of a fixed fee of 150,000 and a variable percentage of 0.02% of the amount over 50,000,001 for each arbitrator.[57] The administrative fee is capped at 21,000 USD for disputes amounting in above 10,000,001 USD).[58]

To ensure that these costs are ultimately paid, Section 18 (1) (c) Arbitration Act, the tribunal can order a claimant to provide security for costs. The applicant for security can also seek the assistance of the High Court to enforce any order made by the Tribunal.

At the end of the arbitration, costs are often reassessed. Usually in arbitral proceedings the prevailing party is entitled to its cost. It may depend on the respective arbitral rules how the costs will be split. In Section 32b (1) Arbitration Act, arbitral tribunals in Kenya are equipped with a wide discretion in that regard which could allow for an allocation of cost to the detriment of one party.

The various costs presented should be taken into account when considering the regulation of Third-Party Funding since the funder could relieve the funded party in that regard.

(d) Stakeholders in arbitration

Different entities may be described as having an interest or a stake in arbitration proceedings (in every case depending on the nature of the issues concerned and the potential outcome of the award on a party). Any legal

[56] NCIA, Domestic Arbitration Fees <https://ncia.or.ke/domestic-arbitration/>.
[57] See NCIA, International Arbitration Fees <https://ncia.or.ke/international-arbitration/> for a staggered table with an overview of the arbitrator's fees depending on the amount in dispute.
[58] NCIA, International Arbitration Fees <https://ncia.or.ke/international-arbitration/>.

reforms may affect arbitration in Kenya should take into account the effect on all these stakeholders:

Parties: the parties to the arbitration themselves naturally have the biggest interest in the result of the arbitration proceeding. Besides monetary, also reputational interests can be touched by the result of an arbitral proceeding. Further, depending on the volume of a case, sometimes the existence of a company can be at stake.

Party Representatives and Stakeholders: Also the parties' representatives usually have a reputational and monetary interest in the outcome of the arbitration. Likewise, the parties' creditors and shareholders have a monetary interest in arbitration proceedings since potential payments can from the party can be dependent on the case.

Arbitrations and Arbitral Institutions: Other stakeholders in arbitration are the arbitrators and the arbitral institution administering the arbitral proceeding. They are usually aiming for a fair proceeding for the parties where neither the proceeding nor the award itself raises the need of a challenge to the parties because of procedural aspects.

The list above is not conclusive but is supposed to help develop an understanding of the range of individuals and entities that may have a direct interest in an arbitration.

(e) An overview of the role of selected stakeholders in the arbitration process

This section provides a brief overview of how the various stakeholders work together and are affected by in arbitration.

The cornerstone of arbitration is party autonomy. This is because the whole proceeding is based on the parties' consent to refer their dispute to arbitration.

It is therefore not surprising that parties to arbitration generally have various possibilities to influence the arbitral proceeding including:

- the number of arbitrators, section 11 (1) Arbitration Act;
- the procedure of appointing the arbitrator(s), section 12 (2) Arbitration Act;
- the procedural rules to be followed by the Tribunal, section 20 (1) Arbitration Act;
- the legal "seat" of the arbitration proceeding, section 21 (1) Arbitration Act;
- the applicable substantial law, section 29 (1) Arbitration Act;
- the geographical place the proceedings should be conducted, section 21 (1) Arbitration Act; and
- the language of the arbitration, section 23 (1) Arbitration Act.

The Tribunal's jurisdiction derives from an effective arbitration agreement by the parties. The Arbitration Act does not expressly exclude subject matters from being arbitrable. However, there is a general understanding that due to public policy, criminal and constitutional matters may not be referred to arbitration.

Because parties are intentionally afforded significant power to control the proceedings, the role of state courts in arbitration is intentionally limited. Generally state courts are not permitted to intervene in matters governed by the Arbitration Act. Limitations on their intervention are provided in section 10 of the Arbitration Act, which only permits intervention in the following situation:

- where the tribunal requests assistance in the taking of evidence;
- where parties institute procedures to challenge the appointment of an arbitrator;
- to determine the tribunal's jurisdiction (after being decided by the tribunal itself in accordance with section 17 of the Arbitration Act (*Kompetenz-Kompetenz*));

- to give interim orders of protection during arbitration; and
- to determine questions of law on application by the parties.

Although these measures seem to allow courts a variety of interference options, because of section 10 of the Arbitration Act these can only be enacted upon the request of a party. In practice, courts in Kenya are generally supportive of arbitration proceedings which is why the likelihood of interferences is rather low.[59] In this regard, Art. 159 (2) of the Constitution should be taken into account. According to the provision, in exercising judicial authority courts should promote alternative forms of dispute resolution including reconciliation, mediation, arbitration and traditional dispute resolution mechanisms.

Furthermore, the courts are competent to decide on appeals and challenges of awards. For international arbitral awards, the only recourse option is an application to set aside to award under the conditions set out in section 35 Arbitration Act. In domestic arbitrations a party can appeal on a point of law arising in the course of arbitration or out of the award to the High Court in accordance with section 39 Arbitration Act. Local awards can also be set aside on grounds provided for in section 35 Arbitration Act. However, party autonomy allows for the exclusion of challenges of arbitral awards within public policy limits.

Summarizing, party autonomy and the will of the parties is given a high priority, as in most jurisdictions, in arbitration in Kenya. Thus, a basic prerequisite for the creation of an internationally attractive arbitration location is fulfilled.

[59] Nikhil Desai/Elizabeth Kageni, *Arbitration procedures and practice in Kenya* (2021) <https://uk.practicallaw.thomsonreuters.com/w-017-2955?transitionType=Default&contextData=(sc.Default)&firstPage=true#co_anchor_a940893>.

III. THE CURRENT KENYAN LAW ON THIRD-PARTY FUNDING

There is no current law expressly permitting or prohibiting Third-Party Funding.[60] Nevertheless, the originally in common law jurisdictions developed doctrines of maintenance and champerty appear to continue to apply in Kenya.[61] As principles having potentially the strongest effect on the legality of Third-Party Funding, they should be analyzed with regard to established practice in other jurisdictions. Before that, to get a better understanding of the legal cultural view on funding of proceedings in general, the legal profession in Kenya with a focus on contingency fees shall be summarized.

(a) The legal profession in Kenya and Contingency fees

The legal profession in Kenya is fused and does not distinguish between solicitors and barristers. Only lawyers admitted to the Bar, referred to as Advocates of the High Court of Kenya, have the right of audience before courts (both superior and subordinate). To be admitted as an advocate, a person must be a citizen of Kenya, Rwanda, Burundi, Uganda or Tanzania (section 12, Advocates Act). Foreign lawyers do not have rights of audience unless they are qualified to practice as advocates in Kenya and have obtained practicing certificates. However, the Attorney-General has discretion to permit a foreign practitioner to practice as an advocate in Kenya in certain cases prescribed by law.[62]

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[60] Feedback of Representative of the Attorney's General Office of Kenya on Research Questions submitted on 11 April 2022

[61] *Ibid*; See Peter Mwangi Muriithi, *Champerty and Maintenance: The Legality of Third-party Funding in Arbitration in Common Law Jurisdictions* (2022) Volume 10, Issue 1 , CiARB Kenyan Branch, Alternative Dispute Resolution Journal, 193.

[62] Nikhil Desai/Elizabeth Kageni, *Arbitration procedures and practice in Kenya* (2021) <https://uk.practicallaw.thomsonreuters.com/w-017-2955?transitionType=Default&contextData=(sc.Default)&firstPage=true#co_anchor_a940893>.

Regarding contingency fees, according to section 46 of the Kenyan Advocates Act, any agreement for the purchase by an advocate of the interest, or any part of the interest, of his client in any suit or other contentious proceeding; any agreement relieving any advocate from responsibility for professional negligence or any other responsibility to which he would otherwise be subject to as an advocate; or any agreement by which an advocate retained or employed to prosecute or defend any suit or other contentious proceeding stipulates for payment only in the event of success in such suit or proceeding, or that the advocate shall be remunerated at different rates according to the success or failure, is invalid. Thereby, contingency fees are in both litigation and arbitration prohibited in Kenya. The prohibition of contingency fees does not directly affect Third-Party Funding but can be considered when evaluating the traditional legal view in regard to funding proceedings.

(b) The doctrines of maintenance and champerty

The doctrines of maintenance and champerty are generally understood as legal concepts prohibiting third parties from funding or profiting from contentious litigation proceedings in which they do not have an interest recognized by law.[63]

Maintenance can be defined as "giving 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." Champerty is defined as "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."[64]

[63] See The Law Reform Commission of Hong Kong, *Third Party Funding for Arbitration* (Report, 2016) 10, 11.

[64] *Bojhary PJ in Winnie Lo v HKSAR* [2012] 15 HKCFAR 16; Some Kenyan authorities quote the UK case of Giles v Thompson for defining maintenance and champerty: "…in modern

The underlying justification for preventing third parties to fund proceedings was traditionally to avoid parties that have no interest in profiting from the litigation proceedings. In other words, there was concern that external funding would result in frivolous or vexatious litigation. Although some jurisdictions still maintenance and enforce the doctrines, like Ireland[65], there are also changes like in Hong Kong and Singapore where both states have introduced legislation to permit and regulate the use of Third-Party Funding in international arbitration.[66]

(c) Exceptions to maintenance and champerty

Since there is no solidified literature accessible regarding the doctrines of maintenance and champerty in Kenya, there is even less so for exceptions of the two principles. Therefore, the exceptions which existed in Hong Kong before the law reform (and currently still exist in litigation)[67] and the current exceptions in Ireland shall be summarized.

1. Hong Kong

Before the reform of 2017, there were mainly three exceptions to the rule against maintenance and champerty established in *Unruh v Seeberger*: (i) the "common interest" category, whereby persons with a legitimate interest in the outcome of the litigation are justified in supporting the litigation; (ii)

idiom maintenance is the support of litigation by a stranger without just cause. Champerty is an aggravated form of maintenance. The distinguishing feature of champerty is the support of litigation by a stranger in return for a share of the proceeds." - See Peter Mwangi Muriithi, *Champerty and Maintenance: The Legality of Third-party Funding in Arbitration in Common Law Jurisdictions* (2022) Volume 10, Issue 1 , CiARB Kenyan Branch, Alternative Dispute Resolution Journal, 193. We consider the definitions provided in the mentioned case as more precise and since the doctrines are originated from common law, we refer to the definitions provided from HK judgments.

[65] In May 2017 the Irish Supreme Court blocked a Third-Party Funder from funding a major case against the Irish state on grounds of champerty, *Persona Digital Telephony Ltd & Sigma Wireless Networks Ltd v. The Minister for Public Enterprise, Ireland, the Attorney General, Denis O'Brien and Michael Lowry,* [2017] IESC 27.

[66] Ashurst Guide, *Third Party Funding in International Arbitration* (1 February 2022) <https://www.ashurst.com/en/news-and-insights/legal-updates/quickguide---third-party-funding-in-international-arbitration/>.

[67] See Chapter 3 for detailed information.

cases involving " access to justice" considerations; and (iii) a miscellaneous category of practices accepted as lawful such as the sale and assignment by a trustee in bankruptcy of an action commenced in the bankruptcy to a purchaser for value. The exceptions still apply for litigation proceedings, where Third-Party Funding has not been excluded of the scope of the doctrines of maintenance and champerty.

Bankruptcy and insolvency have been long-standing exceptions to the doctrines of maintenance and champerty. A liquidator may seek funding from a third party to file a negligence liability claim against the previous management of the company for damages. Also, a trustee may seek funding to commence litigation to recover assets of a bankrupt. For this, the trustee can directly discuss the terms of a funding agreement with a funder without any approval from the court. Likewise, the access to justice exceptions is recognized to help claimants with meritorious claims but insufficient resources to fund litigation.

2. Ireland

In May 2017, the Supreme Court of Ireland ruled that Third-Party Funding is expressly illegal under the doctrine of champerty.[68] Nevertheless, two types of third-party litigation funding are currently allowed. First, the funding of a proceeding by a third party with a legitimate interest in the proceedings, such as a creditor or a shareholder of a company that is a party to the litigation in question is exempted from the doctrines of maintenance and champerty[69] (similar to the first exception applying in Hong Kong). Second, litigation funding based on an "after-the-event"

[68] *Persona Digital Telephony Ltd & Sigma Wireless Networks Ltd v. The Minister for Public Enterprise, Ireland, the Attorney General, Denis O'Brien and Michael Lowry*, [2017] IESC 27; Bench Nieuwveld/Sahani, *Third-party Funding in International Arbitration* (2017), 227.
[69] Colin Monahagan, *Third Party Litigation Funding in Ireland* (24 February 2021) <https://www.mhc.ie/latest/insights/dispute-resolution-update-third-party-litigation-funding-in-ireland#:~:text=Two%20types%20of%20third%20party,to%20the%20litigation%20in%20question>.

insurance policy is allowed. The Third-Party Funder acts as an insurer that provides the coverage. These policies are typically taken-out by a plaintiff after litigation has arisen and are intended to protect the plaintiff if it is unsuccessful in the litigation proceeding. The insurance premium is usually only paid if the plaintiff is successful.

(d) Consequences for breach of the rule against maintenance and champerty

The direct legal consequence of a contract in breach with the doctrines of maintenance and champerty would be invalidity. This would mean that Third-Party Funding agreements which would be in breach of the two doctrines would have to be regarded as invalid. The breach of the rule against maintenance and champerty can potentially further give rise to civil liability.

1. Tortious claims

In case the prohibition of maintenance and champerty would include Third-Party Funding under Kenyan law, the execution of it could be characterized as civil wrongdoing or tort. Thus, where a party proves that an agreement is champertous or constitutes maintenance, the agreement would most likely be held void and unenforceable between the parties.[70]

2. Attorney discipline

In cases where advocates would actively participate in a champertous agreement, their recovery of own costs could be endangered and they might be liable for costs of the defendant. Furthermore, they may be subject to a disciplinary hearing for professional misconduct by the disciplinary tribunal in accordance with section 57 ff of the Advocates Act.

[70] This was the case in Hong Kong before the law reform 2017, see The Law Reform Commission of Hong Kong, *Third Party Funding for Arbitration* (Report, 2016) 44.

(e) Maintenance and champerty in international arbitration under Kenyan law

Since the doctrines of maintenance and champerty were originally established for litigation proceedings, their applicability for arbitral proceedings remains unclear, both in Kenya and other jurisdictions.

Maintenance and champerty were never addressed in various legislative acts concerning the procedural arbitration rules in Kenya even though they were known in Kenya as part of its common law tradition. Some legal authorities argue that this omission gives a "*wide berth*" to the issue of Third-Party funding.[71] This assessment would imply "*that third-party funding in arbitration is not outlawed and/or illegal*".[72]

This assessment is not necessarily persuasive. A decision not to directly regulate champerty and maintenance could also be interpreted as a sign that legislators did not believe there was any reason to regulate Third-Party Funding because it was already prohibited. This analysis can be supported with the definitions of maintenance and champerty which covers most concepts of Third-Party Funding.

Some authors consider the doctrines of maintenance and champerty as outdated and should therefore not be applied to prohibit Third-Party Funding because the doctrines no longer reflect public policy anymore.[73] Despite this view, the scope of the doctrines cannot be ignored. If a court would follow a strict interpretation of the doctrines, it could argue that as

[71] See Peter Mwangi Muriithi, *Champerty and Maintenance: The Legality of Third-party Funding in Arbitration in Common Law Jurisdictions* (2022) Volume 10, Issue 1, CiARB Kenyan Branch, Alternative Dispute Resolution Journal, 193.
[72] *Ibid.*
[73] Fahad Bin Siddique, Champerty vs. Third-Party Funding in Arbitration, A Censorious Debate, SCLS Law Review Vol. 3. No.3 [Sept 2020].

long as the doctrines are not regulated, they have to be applied as part of the legal regime of the respective state.[74]

Furthermore, although they were most likely originally established for litigation proceedings, an unconditional limitation of the scope for litigation and an exclusion for arbitration cannot be simply assumed. This again is dependent on how a court would concretely interpret the two doctrines.

Therefore, it has to be summarized that the applicability of the doctrines remains ambiguous, with good arguments for being applicable considering the scope generally understood in regard to the doctrines of maintenance and champerty. This ambiguity can only be demolished by regulation or a high court judgment. A simple inapplicability should not be assumed.

1. Annulment, recognition and enforcement of the award

The doctrines of maintenance and champerty can also endanger the enforceability of an award made for a case in which one of the parties has been funded by a Third-Party Funder. The award could be annulled and the enforcement of the award can be denied because of public policy reasons both for international due to Article V (2) (b) of the New York Convention and domestic arbitration due to section 35 (2) (b) (ii), 37 (1) (b) (ii) of the Arbitration Act in Kenya.

Although this outcome may theoretically be possible, there are several reasons to question whether a denial of recognition or enforcement or an annulment of the award would realistically be the practical outcome in cases where third-party funding would occur against the doctrines of maintenance and champerty.

It could be argued that an award could be annulled if the law of the arbitral seat prohibits third-party funding under maintenance and champerty. This

[74] In *Unruh v Seeberger* (2007) the Final Court of appeal made it clear that it is for the legislature to change the Hong Kong law to clearly allow Third-Party Funding for arbitrations taking place in Hong Kong, if it considers it to be appropriate to do so.

could already be doubted through questioning the applicability of local prohibitions based on champerty and maintenance in international arbitration.[75] Furthermore, even if the application of the substantive prohibitions would be assumed, it remains uncertain what, if any, effect those substantive prohibitions would have on arbitral proceedings themselves or on resulting awards.[76] For annulling an award, generally only the mandatory procedural law and not the mandatory substantive law is decisive. The doctrines of maintenance and champerty are traditionally regarded as substantive law.[77] Substantive law can exceptionally be the basis for the annulment of an award if the application of that law in an award violates public policy. The doctrines of maintenance and champerty however are aimed at the funding agreement itself but not generally at the outcome of the funded dispute. The public policy element of the doctrines of maintenance and champerty would thereby generally aim at the underlying agreement and not at the outcome of the dispute funded. This limited remedy is justified to avoid affecting parties who are unrelated to or even unaware of an original champerties agreement.[78]

Under similar reasoning, it is unlikely that a jurisdiction, in which the doctrines of maintenance and champerty exist in full force, would refuse the recognition and enforcement of an arbitral award because a party received outside funding. Only a court interpreting the mere presence of a third-party funder as contaminating the award with a public policy violation would justify the refusal of recognition and enforcement of the award.[79]

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[75] "Even before England expressly permitted third-party funding in litigation, English courts acknowledged that the doctrine of champerty did not extend to arbitral proceedings" - Catherine A. Rogers, *Ethics in International Arbitration* (2014), 191.
[76] *Ibid.*
[77] *Ibid.*
[78] *Ibid.*
[79] The possibility of a refusal of an award on public policy grounds due to maintenance and champerty for international awards is disputed with the argument that champerty does not relate to the arbitral award but only to the relation between the funder and the funded party, see Catherine A. Rogers, *Ethics in International Arbitration* (2014), 192.

Although practical consequences for the arbitral award in cases of the existence of Third-party Funding agreements seem unlikely, it cannot be excluded that courts in Kenya would interpret this issue differently. Therefore, it cannot be excluded that a court at the place of enforcement or at the seat may decide that the existence of a funding agreement is a public policy issue relevant to the annulment, recognition and enforcement rules under the New York Convention.[80] Such a decision may even be policy driven, if the court would take into account that an effective prohibition of Third-Party Funding may require the annulment or the non-enforcement of an award in cases in which a party was funded if the parties of the funding agreement would choose a law for the funding contract which does not prohibit Third-Party Funding (see next paragraph).

2. Avoidance of Third-Party Funding prohibitions in international arbitration

A great limitation of the possibility of Third-Party Funding or uncertainties about the legality of it could invite parties to try to avoid the application of Kenyan law and an enforcement in Kenya in the first place. This could be organized with the options granted to the parties when drafting the arbitration agreement[81] and the funding agreement. Funding agreements are ancillary to arbitration agreements and therefore do not generally have any formal relationship to the legal seat.[82]

Firstly, the parties of the funding agreement itself could therefore exclude the applicability of Kenyan law and thereby the applicability of the doctrines of champerty and maintenance. Furthermore, the funding agreement could separately designate that an arbitration arising out of the funding

[80] Nieuwveld and Shannon, Third-Party Funding in International Arbitration 13
[81] See II. (e).
[82] Catherine A. Rogers, *Ethics in International Arbitration* (2014), 193.

agreement itself be seated in a jurisdiction in which Third-Party Funding is permissible.[83]

Careful planning can ensure that both the award and the funding agreement escape potential scrapes with national prohibitions in Kenya. Nevertheless, if the parties would try to enforce an award, the ambiguity in regard of a Kenyan judge's perspective in relation to public policy issues explained in the paragraph above remains.

[83] Ibid.

CHAPTER 3

REGULATION OF THIRD-PARTY FUNDING FOR ARBITRATION IN OTHER COMMON LAW JURISDICTIONS

I. INTRODUCTION: THE REGULATION OF THIRD-PARTY FUNDING IN DIFFERENT STATES

Recent reforms in other jurisdictions to regulate Third-Party Funding are relevant to Kenya. Specifically, other common law jurisdictions have been reducing or eliminating the doctrines of maintenance and champerty to allow Third-Party Funding and developing specific regulations that apply directly to Third-Party Funding and attorneys working with funders.

First, this section begins with a focus on funding in England. Specifically, this section provides case studies on the emergence and the evolution of Third-Party Funding in England, which is one of the most developed Third-Party Funding markets.

Next, this section examines recent developments in Singapore and Hong Kong. These are both common law jurisdictions that have recently enacted legal reforms to legalize Third-Party Funding, but also to ensure the effective use of funding in international arbitrations seated in those jurisdictions.

Finally, this section addresses recent developments in Nigeria and South Africa. These jurisdictions are particularly useful in understanding the possible impacts of Third-Party Funding in African countries. Both Nigeria and South Africa do not yet have specific legislation regarding Third-Party Funding. Nevertheless, both jurisdictions are actively examining issues relating to Third-Party Funding as a result of the large volume of foreign

investments in Africa, and related efforts to make African jurisdictions more competitive in international arbitration.

Proponents of Third-Party Funding argue that it could be a great instrument to increase foreign investment, promote access to justice, and make jurisdictions that permit it attractive venues for international arbitration. On the other hand, it can weaken the parties' and lawyers' control over litigation because the funders can be expected to try to exert control over strategic decisions; it might also compromise the attorney-client relationship by diminishing the professional independence of attorneys due to the presence of a third-party into disputes.[84]

While several jurisdictions are moving to expressly permit Third-Party Funding, many of those jurisdictions are also seeking to enact affirmative regulations to ensure it operates properly: there is not a general acceptance to leave Third-Party Funding wholly unregulated.

Jurisdictions that have regulated Third-Party Funding have also considered whether to permit it only for international arbitration or also to allow it for domestic arbitration. This distinction could also be an important consideration for Kenya in light of potential effects on access to justice in domestic Kenyan disputes.

II. ENGLAND AND WALES

This section examines the historical development and modern treatment of Third-Party Funding in England and Wales.

(a) Third-Party Funding in litigation

Historically, Third-Party Funding was prohibited by the doctrines of maintenance and champerty. As previously analyzed, third-party

[84] Yourtcp.com. 2019. *The Pros and Cons of Litigation Funding*. <https://yourtcp.com/wordpress/?p=891>

involvement in lawsuits was understood as potentially discrediting the purity of justice by manipulating evidence in exchange for potential personal gain.[85]

Despite these prohibitions, there has been a progressive judicial approval of litigation funding. The modern history of Third-Party Funding in England and Wales dates to 1967: maintenance and champerty were formally abolished as crimes and torts by Section 13 of the *Criminal Law Act 1967*. The explanation for this revolution was the recognition by the Law Commission of the importance of financial assistance in exercising the right to access to justice.[86] However, while the Legislator abolished these crimes, the possibility of funding litigation for profit was in fact limited: success-based lawyers' fees were in fact prohibited at the time, while the legal aid system was quite functional. Conditional Fee Arrangements, by which lawyers could get an upscale premium if the case is won, were introduced by the Courts and Legal Services Act in 1990.[87] Conditional Fees differ from contingency fee agreements, where the lawyer may share in an agreed percentage of the sum recovered by the client with no direct correlation to the work done.[88]

After the 2000s, it was stated that Conditional Fee Agreements could be charged to the counterparty, rather than to the lawyers' own client[89]: liability insurers were concerned about the potential increase in their disbursements.

After this formal legal change, English courts have increasingly adopted the view that the modern judicial system is strong enough to avoid the risk of

[85] see Chapter 2, III, (b)
[86] Law Commission for England and Wales, 1966. *Proposals for the Reform of the Law Relating to Maintenance and Champerty*, Report No 7, p. 5
[87] Solas, G., 2017. *Third Party Litigation Funding: a comparative analysis*. Iris.unica.it. <https://iris.unica.it/bitstream/11584/248711/2/Tesididottorato_GianMarco_Solas.pdf>
[88] Mlaw.gov.sg. 2022. *No Win No Fee: Contingency Fee Lawyers in Singapore*. <https://www.mlaw.gov.sg/news/press-releases/2022-04-29-framework-cfas-in-singapore-commence-4-may-2022#fn1>
[89] Access to Justice Act 1999, §27 and §29

abuse of process[90] against which the doctrines of maintenance and champerty were designed to protect.[91]

Over the years, the common feeling that the costs of justice were too high has certainly helped the favorable perception towards the possibility to fund litigation.[92] In 2003, the English Court of Appeal in *R (Factortame) Ltd v Secretary of State for Transport, Local Government and the Regions* held that a funding agreement for litigation proceedings would not be automatically considered contrary to public policy: it should be decided on a case-by-case basis.

The symbolic shift in the UK case law concerning Third-Party Funding is commonly represented by *Arkin v Borchard Lines Ltd* case in 2005. The Court of Appeal explicitly approved Third-Party Funding in litigation in the interests of ensuring access to justice, affirming that a funder is liable to the other party only to the extent of its funding.

(b) The Association of Litigation Funders

Today, there is no statutory law regulating Third-Party Funding in England and Wales. Nevertheless, many professional Third-Party Funders are present at the scene: they set up the Association of Litigation Funders and launched a voluntary code of conduct to self-regulate their activity.

The essence of most funding agreements is the funder's promise to pay the claimant's legal costs in exchange for a share in case of victory. Additional terms and conditions are also often negotiated by the parties.[93]

As seen above, this sector is predominantly self-regulating, with some funders volunteering to be members of the Association of Litigation Funders

[90] *Giles v Thompson* [1994]
[91] 2015. *Third Party Funding for Arbitration*. Hong Kong: Third Party Funding for Arbitration Sub-Committee, p. 68
[92] Solas G., *op. cit.*
[93] Latham, S. and Rees, G., 2021. *The Third Party Litigation Funding Law Review - The Law Reviews*. [online] Thelawreviews.co.uk. Available at: <

which sets out for its members certain minimum requirements for Third-Party Funding.[94] The Association of Litigation Funders (ALF) is the independent body appointed by the Ministry of Justice to deliver self-regulation of litigation funding in England and Wales. Although ALF membership is voluntary, most established third-party funders in London have joined. Litigants who contract with ALF members are protected by the *Code of Conduct for Litigation Funders (ALF Code)* enacted in 2011.

Some of the main features of the ALF Code are capital adequacy requirements, limitations on the withdrawal of funding during litigation, and limitations on the Third-Party Funder's ability to influence litigation. In particular, all funder members of the ALF must have a minimum of £5 million of capital and are verified by a third party as able to cover their liabilities for 36 months[95], they cannot terminate the funding agreement at their discretion and they cannot take any steps that cause or are likely to cause the funded party's lawyers to act in breach of their professional duties. Furthermore, funders cannot seek to influence the funded party's lawyers to cede control or conduct of the dispute to them.[96]

There is no general requirement under English law for a party to disclose a Third-Party Funding arrangement to other parties, the court or tribunal. It is moderated only by the tribunals' power to order disclosure.

The self-regulation approach through the voluntary ALF Code used in the UK has come under some criticism. For this reason, in 2012 the following amendment was moved:

> *Require any person which enters into a Third-Party Funding agreement with a litigant to first obtain a license from a licensing body*

[94] Petit, S. and Kajkowska, E., 2019. *Developments in third party funding in arbitration*. Nortonrosefulbright.com. <https://www.nortonrosefulbright.com/en-gb/knowledge/publications/c015054d/developments-in-third-party-funding-in-arbitration>

[95] Rule 9.4.1.2 of the ALF Code

[96] Rule 9.3 of the ALF Code

to be designated by the Lord Chancellor, and set out conditions to be satisfied in order to obtain such a license.

Despite the effort, the amendment was not approved as the Third-Party Funding was still considered irrelevant.

III. SINGAPORE

(a) The pre-reform period

Historically, Singapore law prohibited Third-Party Funding under the doctrines of maintenance and champerty. Nevertheless, Singapore Courts were inclined to allow Third-Party Funding when the funding agreement came from a party with a genuine commercial interest in the litigation and there was no evidence that the funder would influence the action.[97] The need was to protect the integrity and the proper course of justice in Courts: for this reason champertous arrangements were almost always spoken concerning litigation proceedings.

In 2006 there was an extension in the scope of application of the doctrines of champerty and maintenance. In *Otech Pakistan Pvt Ltd vs. Clough Engineering Ltd,*[98] the Singapore Court of Appeal ruled that the doctrine of champerty applies also to international arbitration proceedings as a form of litigation. The decision dispels the conception that the doctrines of champerty and maintenance have only an ethical nature: they are part of public policy. It should apply every time an agreement would pose a danger to the proper administration of justice, even when parties have chosen a private dispute resolution system like arbitration.[99]

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[97] 2015. *Third Party Funding for Arbitration*. Hong Kong: Third Party Funding for Arbitration Sub-Committee

[98] *Otech Pakistan Pvt Ltd vs. Clough Engineering Ltd* [2007]

[99] Boo, L., 2007. *Arbitration Law*. Academypublishing.org.sg. <https://academypublishing.org.sg/Journals/Singapore-Academy-of-Law-Annual-Review-

(b) Regulation of Third-Party Funding

The extension of the scope of the doctrines of champerty and maintenance to arbitration proceedings had a risk of making Singapore less attractive for international arbitrations. In particular, it had the greatest impact on commercial arbitrations since they are usually more onerous for parties. For these reasons, there have been several legislative changes since 2017 to make Singapore more attractive to foreign investors.

The *Civil Law (Amendment) Act* (i.e., CLAA) came into force in 2017. The CLAA abolishes the maintenance and champerty as regards dispute resolution proceedings. The meaning of dispute resolution proceedings is defined by the *Civil Law (Third Party Funding) Regulations*, which came into force together with the CLAA. According to Section 3, dispute resolution proceedings are arbitration, mediation proceedings and any other actions connected with them.

The Regulations brought some standards for the qualification of Third-Party Funders, which include activity and financial requirements: the idea is to limit funding activity to professional bodies that are financially stable. Indeed, according to Section 4, Third-Party Funders must:

> • *Carry on the principal business, in Singapore or elsewhere, of the funding of the dispute resolution proceedings to which the Third-Party Funder is not a party; and*
>
> • *Have a paid-up share capital of not less than $5 million or the equivalent amount in foreign currency or not less than $5 million […]*

Every qualifying Third-Party Funder must comply with the requirements prescribed by the Minister (v. Section 5(B)(8) of the CLAA). In case of non-

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of-Singapore-Cases/e-Archive/ctl/eFirstSALPDFJournalView/mid/512/ArticleId/190/Citation/JournalsOnlinePDF>

compliance with the mandatory requirements, the rights of the Third-Party Funders are not enforceable (v. Section 5(B)(A) of the CLAA). However, Section 5(B)(5) states that Third-Party Funders can apply to a court or arbitral tribunal for relief from this sanction brought by the law.

Additionally, solicitors are prohibited from entering into contingency fee agreements with their clients (v. Section 5(B) of the CLAA). However, the CLAA amends Section 107 of the *Legal Profession Act* to permit Singapore legal practitioners to:

- Introduce, or refer, third party funders to their clients, so long as the legal practitioner does not receive any direct financial benefit from the introduction or referral; and

- Advise on, negotiate, draft, and act in a dispute arising out of and/or in connection with their client's third-party funding contract.

Over the years, this position has proven to be against other common law jurisdictions' views[100]. From 4 May 2022, lawyers in Singapore can enter into conditionals fee agreements in selected proceedings thanks to the *Legal Profession (Amendment) Act 2022*. Mirroring the recently enacted Third-Party Funding regime in Singapore, Conditional Fee Agreements are permissible in the same categories of proceedings:

- international and domestic arbitrations;
- Singapore International Commercial Court proceedings; and
- related court and mediation proceedings.[101]

[100] See Chapter 3, II, (a)

[101] Mayerbrown.com. 2022. *Conditional Fee Agreements (CFAs) permitted in Singapore from 4 May 2022*. <https://www.mayerbrown.com/en/perspectives-events/publications/2022/05/conditional-fee-agreements-cfas-permitted-in-singapore-from-4-may-2022>

Contingency fee arrangements, where lawyers are paid for their legal fees only if their client's claim is successful, continue to be prohibited in Singapore. On the other hand, Conditional Fee Agreements are permitted but applicable to a limited category of legal proceedings.

This significant development brings Singapore closer in line with the position of other global dispute resolution centers and further strengthens Singapore's position as a leading seat for international arbitration.[102]

IV. HONG KONG

(a) The pre-reform period

Like Singapore, Third-Party Funding in Hong Kong was historically prohibited in both litigation and arbitration by the doctrines of maintenance and champerty. The first judicial recognition came in 1995. In *Cannonway Consultants Limited v. Kenworth Engineering Ltd*, Hong Kong's High Court held that although champerty did apply to litigation proceedings in Hong Kong, it should not be extended to arbitration, because that would mean extending it from the public justice system to the private consensual system which is arbitration.[103]

Notwithstanding the above-mentioned ruling, in *Unruh v. Seeberger (2007)* the Court of Final Appeal did not object Third-Party Funding for arbitration when it was conducted in a jurisdiction where the doctrines of maintenance and champerty did not exist.[104] Nevertheless, this case left open the question of whether champerty and maintenance applied to agreements concerning arbitrations taking place in Hong Kong, contrary to what was

[102] Mlaw.gov.sg. 2022. *No Win No Fee: Contingency Fee Lawyers in Singapore*. <https://www.mlaw.gov.sg/news/press-releases/2022-04-29-framework-cfas-in-singapore-commence-4-may-2022#fn1>
[103] Deacons - Law Firm - Hong Kong. 2016. *Third Party Funding for Arbitrations*. <https://www.deacons.com/2016/03/01/third-party-funding-for-arbitrations/>
[104] *Unruh v. Seeberger* [2007] (Court of Final Appeal) at para 118-119

previously established. It has to be mentioned that the Court identified three exceptions to the prohibition to Third-Party Funding agreements seated Hong Kong:

(i) when the Third-Party Funder has a legitimate interest in the litigation;
(ii) when cases involve "access to justice" concerns; and
(iii) in insolvency proceedings.[105]

Furthermore, the Court of Final Appeal highlighted that it was for the legislature to change the Hong Kong law to allow or not Third-Party Funding for arbitrations taking place in Hong Kong.[106]

(b) Regulation of Third-Party Funding

At about the same time Singapore undertook its Third-Party Funding reforms, Hong Kong undertook a similar reform effort. On 1 February 2019, Hong Kong adopted the *Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Ordinance* together with the *Code of Practice for Third-Party Funding of Arbitration*, permitting Third-Party Funding in arbitration and mediation[107] but it remains prohibited in Hong Kong domestic litigation.

The Ordinance opens by specifying the objectives and giving a definition of Third-Party Funding. According to Section 98E, the purpose of the Ordinance is to ensure Third-Party Funding in all arbitration proceedings, overcoming past judicial contradictions. Moreover, Section 98G subordinates the definition of Third-Party Funding in arbitration to the receipt of a financial benefit for the Third-Party Funder. Consequently, if a

[105] *Unruh v. Seeberger* [2007] (Court of Final Appeal); see also Chapter 3, III, (c), 1
[106] *Unruh v. Seeberger* [2007] (Court of Final Appeal) at para 123 and *Winnie Lo v. HKSAR* [2012] (Court of Final Appeal) at paras 177-179
[107] Petit, S., Chung, K., Proudfoot, C. and Teo, J., 2021. *Third Party Funding in the Asia-Pacific*. Nortonrosefulbright.com. <https://www.nortonrosefulbright.com/en/knowledge/publications/0ac96d60/third-party-funding-in-the-asia-pacific>

funder finances a case without any return in the award (e.g., donation), it will not constitute Third-Party Funding and it will not fall under the scope of this discipline. Therefore, Division 3 of the Ordinance states that the torts of champerty and maintenance do not apply to Third-Party Funding in arbitration.

The Ordinance was accompanied by a detailed Code of Practice for Third-Party Funding of Arbitrations. The Code of Practice sets out specific requirements for funding agreements including provisions to address: the capital adequacy of the funder, effective procedures for managing conflicts of interest and complaints against the funder. In particular, a Third-Party Funder must maintain access to a minimum of HK$20 million of capital, not take any steps that cause the funded party's legal representative to act in breach of its professional duties, disclose conflict of interest to funded parties and ensure that complaints from a funded party in connection to the funding agreements are handled in a timely and appropriate way.[108] As stated in Division 4 of the Ordinance, the Code of Practice is not mandatory for funders: it works as a guideline. A failure in complying with its provision does not render any person automatically liable for any judicial or other proceedings.[109]

Therefore, the Ordinance excludes lawyers from funding: it means that they cannot benefit from the exemption of the maintenance and champerty doctrines in the same way funders benefit[110]. Put differently, nowadays contingency fee arrangements are subject to common law doctrines. Given the widespread prevalence of arbitration, the Hong Kong government's working on the *Arbitration and Legal Practitioners Legislation (Amendment) Bill 2022*. Whilst there is a lot of detail in the Bill, which is widely expected to become law later this year, it will

[108] *Code of Practice for Third Party Funding of Arbitration* at para 2.5, 2.6, 2.18
[109] Carlstedt, C., 2019. *And then there were three… Third party funding in Hong Kong*. [online] Arbitration Blog. <http://arbitrationblog.practicallaw.com/and-then-there-were-three-third-party-funding-in-hong-kong/>
[110] Division 3, Section 98O of the Ordinance

amend the Arbitration Ordinance and Legal Practitioners Ordinance to allow for certain agreements between clients and their lawyers. The new outcome-related fee structures allow lawyers to charge for arbitration work based on conditional fee agreements.[111] The Bill will remove the prohibition on success fees contained in the Ordinance. Moreover, the new law will allow Hong Kong-based lawyers to charge success fees for arbitrations seated in or outside the territory. Lawyers and clients outside Hong Kong can take advantage of the new rules when working on a Hong Kong-seated case.[112]

The new Third-Party Funding regime equates Hong Kong's position with other common law States' lines, with clear evidence of the ongoing horizontal regulatory competition to become increasingly attractive venues for arbitration proceedings. Therefore, it increases funding options for clients and improves access to justice for impecunious parties.

V. A COMPARISON OF SINGAPORE AND HONG KONG REFORMS IMPLICATIONS

At first sight, we can notice that Singapore and Hong Kong reforms have abolished maintenance and champerty to allow Third-Party Funding in arbitration.

Moreover, both jurisdictions have adopted new legislation using a light-touch approach. The term light-touch refers to policy approaches aimed at creating a minimal regulatory environment, rather than a strict one. This

[111] Lau, S., 2022. *Outcome-related Fee Structures in Hong Kong to Provide Flexibility to Those Involved In Construction: Clyde & Co*. Clydeco.com. <https://www.clydeco.com/en/insights/2022/04/flexible-fee-structures-in-arbitration-set-to-furt#_ftn1>

[112] Sanger, K. and Young, B., 2022. *Pays to win – Hong Kong arbitrations set for success fee shake-up*. Herbert Smith Freehills | Global law firm. <https://www.herbertsmithfreehills.com/latest-thinking/pays-to-win---hong-kong-arbitrations-set-for-success-fee-shake-up>

type of approach is justified by the fact that Third-Party Funding is relatively recent phenomenon and governments are not aware of any specific concerns about the activities of Third-Party Funders. The idea is that with judicial supervision in place, there is no need to introduce extra regulation. In common law jurisdiction the legal sources can be found in case-law.[113] Nevertheless, judicial oversight has limits: it cannot guarantee timely and comprehensive regulatory reforms and it is absent when disputes do not arise.[114]

Unlike Singapore, Hong Kong published a separate Code of Practice. While litigation proceedings have been excluded from the new rules in both States, the requirements touch on common points such as minimum capital to be required to be guaranteed by the Third-Party Funders.

Nevertheless, there is a significant difference regarding non-compliance. In Singapore, non-compliance has serious consequences for funders since they would lose their rights under the funding agreement by default, while in Hong Kong, non-compliance does not lead to any serious consequences automatically. This difference shows that, in Hong Kong, the regulation is more flexible: it acts as guidelines.

Furthermore, in both jurisdictions lawyers were excluded from Third-Party Funding rules. The idea was to exclude the possibility of contingency fee agreements because they were considered contrary to public policy and the doctrines of champerty and maintenance. The idea is to prevent a lawyer from having financial interests in a proceeding. Despite this, already at the requests of England and Wales, conditional fee agreements have recently been legalized. This shows how little by little different common law jurisdictions are trying to standardize their legislation and regulate Third-

[113] Gardner, J., 2007. Some Types of Law. *Common Law Theory*, pp. 66-67
[114] Zhang., B., 2021. *Third Party Funding for Dispute Resolution*. Springer Singapore, p. 52

Party Funding to become increasingly attractive arbitration centers for investors.

VI. SOUTH AFRICA

(a) Overview of Third-Party Funding

Despite the fact that it is a common law system, courts in South Africa have determined that Third-Party Funding is permitted under South African law. However, South Africa has not adopted any legislation or regulations to directly govern this practice.

In *Price Waterhouse Coopers v. National Potato Co-operative Ltd (2004)*, the Supreme Court of Appeal of South Africa recognized that the constitutional right to access to justice is often limited by financial constraints and that Third-Party Funding arrangements can provide an opportunity to assist in this regard.[115] In that case, the Court held that financial assistance for litigation in return for a share was not contrary to public policy. The Supreme Court of Appeal relaxed the application of the doctrines of maintenance and champerty only in litigation proceedings[116]: the Court affirmed that funding agreements were looked upon with disfavor unless it could be determined that the financial assistance was offered in good faith in return for a reasonable recompense or interest in the suit.[117] Based on this reasoning, the Court held that Third-Party Funding must not be used for purposes that prejudice another party.[118] Indeed, the Court did qualify this holding by saying that Third-Party Funding arrangements are

[115] *Price Waterhouse Coopers v. National Potato Co-operative Ltd* [2004], para 27
[116] Lawrence, L., 2018. *Regulating third party funding in arbitrations held within south africa*. <https://etd.uwc.ac.za/bitstream/handle/11394/6408/2829-3427-1-RV.pdf?sequence=1&isAllowed=y>
[117] *Price Waterhouse Coopers v. National Potato Co-operative Ltd* [2004], para 27
[118] Hambury, J. and Lewis, D., 2021. *Jurisdiction Guide to Third Party Funding in International Arbitration*. Pinsentmasons.com. <https://www.pinsentmasons.com/out-law/guides/third-party-funding-international-arbitration>

not contrary to public policy in the absence of an abuse of process[119] identified in three instances: frivolous claims, claims instituted to pursue an alternative motive and claims instituted to prejudice the defendant.[120]

Recently, the High Court of South Africa has expanded and deepened what was previously said. In the *De Bruyn v. Steinhoff International Holdings NV case*, the Court held that in order to assess if Third-Party Funding is acceptable, courts have to take into account if:

- the Third-Party Funding arrangement is necessary to provide access to justice;
- the Third-Party Funding arrangement is fair and reasonable in protecting the interests of the defendants;
- the Third-Party Funding arrangement overcompensates or not the Third-Party Funders for assuming the risks of the litigation;
- the Third-Party Funding arrangement interferes or not with the duty of the lawyers to act in the best interests of their clients or the client's rights to exercise control over the litigation; and
- the funded party is able to give instructions and exercise control over the litigation.[121]

The Court also held that the Third-Party Funders should be entitled to lawfully terminate the Third-Party Funding arrangement, where the dispute lacks reasonable prospects of success. However, the opinion of the class attorneys and counsel is required for the termination. The purpose of doing so is to create sufficient safeguards that the funding commitments could not be "*capriciously withdrawn and that funding will remain available to maintain access to the courts*".[122]

[119] *Ivi*, para 52
[120] *Ivi*, para 50
[121] *De Bruyn v. Steinhoff International Holdings NV* [2018], para 82
[122] *Ivi*, para 103

Under these precedents, Third-Party Funding was recognized as valid and permissible in litigation in South Africa based on a recognition of the importance of funding agreement to provide access to justice. For this reason, until recently, there were no efforts to directly regulate Third-Party Funding in South Africa. Furthermore, there are no case studies regarding the possibility of admitting funding agreements in arbitration proceedings.

Unlike the previous States analyzed, in South Africa contingency fee agreements are regulated by *the Contingency Fees Act (CFA) 66* of 1997. Under the Contingency Fees Act, a contingency fee agreement can take one of two forms. The agreement may entitle an attorney to a normal fee for services rendered if the client's claim is successful. In this case, there are no limitations on the amount. Otherwise, the agreement may entitle the attorney to a success fee, in addition to the normal fee: in this case there are limitations.[123]

(b) Regulation of Third-Party Funding in arbitration

The Arbitration Foundation of Southern Africa (AFSA) is one of the leading arbitral institutions in South Africa. AFSA has recently published a set of international arbitration rules (i.e., the Rules), which came into effect on 1 June 2021. AFSA is the body responsible for the administration of disputes in accordance with the Rules, and other procedures or rules agreed upon by the parties. As stated in the preamble, when the parties have agreed in whatsoever manner for arbitration under the AFSA Rules, they shall be taken to have agreed that any arbitration between them shall be conducted in accordance with them.

In particular, Article 27 allows Third-Party Funding arrangements for international arbitrations administered by AFSA. A "Third-Party Funder" is

[123] DSC Attorneys. 2021. *Lawyers' Contingency Fees in South Africa: What Does "No Win, No Fee" Mean?*. <https://www.dsclaw.co.za/articles/lawyers-contingency-fees-in-south-africa-what-does-no-win-no-fee-mean/>

defined as any natural or legal person who is not a party to the arbitration, but who agrees with a party to provide material or financial support for all or part of the costs of the arbitration. It could be constituted through donation, grant or in exchange for remuneration or reimbursement dependent on the outcome of the arbitration. Furthermore, the existence of a Third-Party Funding agreement and the identity of the Third-Party Funder must be disclosed to the other parties, to the arbitration as well as to the arbitral tribunal and the AFSA Secretariat.[124]

Despite this initial recognition, such effort is not as effective as a legislative act. As such, it cannot be generally applied to all arbitration proceedings, but it must be expressly requested by the parties. Consequently, there is less protection for parties because no special requirements are placed on Third-Party Funders in terms of, for example, financial prerequisites.

VII. NIGERIA

(a) Overview of Third-Party Funding

Like other common law jurisdictions, the doctrines of champerty and maintenance apply in Nigeria, unless they are expressly abolished or modified by legislation or case law.[125] Several decisions in Nigerian cases demonstrate that Courts still regard Third-Party Funding in litigation proceedings as champertous.

In the *Oloko v. Ube* case,[126] the Nigerian Court of Appeal held as follows:

[124] Lafleur, J., Herholdt, T. and Shein, R., 2021. *South Africa: Third party funding under the new AFSA International Arbitration Rules*. Bowmans. <https://www.bowmanslaw.com/insights/litigation-and-arbitration/south-africa-third-party-funding-under-the-new-afsa-international-arbitration-rules/>

[125] Omoaka, G., Nweke-Eze, S. and Odunsi, O., 2021. *Third-party funding in Nigeria-seated arbitration proceedings*. Ibanet.org. <https://www.ibanet.org/third-party-funding-Nigeria-arb-proceedings>

[126] *Oloko v. Ube* [2001]

> *"An agreement by a solicitor to provide funds for litigation in consideration of a share of the proceeds is champertous. The solicitor cannot recover from his client his own costs or even his out-of-pocket expenses".*

In particular, this case excluded any possibility of using contingency fees by lawyers. This position was certainly in line with the old idea of most common law countries. As seen, however, recently many of these States have abandoned this approach to allow at least conditional fee agreements.

Later in 2015, the Nigerian Court of Appeal in *Egbor & Anor v. Ogbebor* also found a funding arrangement was champertous:

> *"[…] a situation where a person elects to maintain and bear the costs of an action for another in order to share the proceeds of the action or suit is champertous*".[127]

Lacking a clear statutory or case law governing Third-Party Funding in arbitration proceedings, the holding in *Egbor & Anor v. Ogbebor* suggests that traditional funding relationships may be held to be champertous.[128]

(b) Regulation of Third-Party Funding in arbitration

The *Arbitration and Conciliation Act 1988* (i.e., ACA) is the main legislation governing arbitration in Nigeria. The *Arbitration and Mediation Bill 2020* (i.e., the Bill) has been proposed by the Nigerian legislative organ to amend the ACA and to provide a legal framework for efficient settlement of commercial arbitration and it comprises certain provisions aimed at encouraging Third-Party Funding.

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[127] *Egbor & Anor v. Ogbebor* [2015], paras A–D

[128] Omoaka, G., Nweke-Eze, S. and Odunsi, O., 2021. *Third-party funding in Nigeria-seated arbitration proceedings*. Ibanet.org. <https://www.ibanet.org/third-party-funding-Nigeria-arb-proceedings>

The Bill, which is passing through the final stages of the Nigerian legislative process, legalizes Third-Party Funding in arbitration (but not litigation) in an indirect way.

Section 61(1) of the Bill expressly abolishes the torts of maintenance and champerty concerning Nigeria-seated arbitration proceedings.

Furthermore, the Bill incorporates the costs of obtaining Third-Party Funding as part of the costs for arbitration (v. Section 52(1)(g) of the Bill). In other words, the Bill does not expressly state that Third-Party Funding will be legal, but the consequence of including it as part of the costs of arbitration logically means that the Bill has tacitly permitted Third-Party Funding.

Additionally, Section 62(1)(1) of the Bill compels the party benefitting from a Third-Party Funding arrangement to *"give notice to the other party or parties, the arbitral tribunal and, where applicable, the arbitral institution, of the name and address of the Third-Party Funder".*[129]

Additionally, Section 91(1) of the Bill defines the concept of Third-Party Funder: *"Third-party funder means any natural or legal person who is not a party to the dispute but who enters into an agreement either with a disputing party, […] in order to finance part or all of the cost of the proceedings, […] and such financing is provided either through a donation or grant or in return for reimbursement dependent on the outcome of the dispute or in return for a premium payment".*[130] This definition is quite consistent with the international standard regarding funding agreements; however, following a deep analysis it should be noted that the Bill includes "donation" in such definition. By contrast, other common law jurisdictions (such as Hong Kong[131]) stated that if a funder finances a case without any return in the award, this will not constitute Third-Party Funding. This difference has practical consequences: if a donation is considered a Third-

[129] Section 62(1)(1) of the Arbitration and Mediation Bill [2020]
[130] Section 91(1) of the Arbitration and Mediation Bill [2020]
[131] See Chapter 4, III, (b)

Party Funding agreement, the party must fulfill the conditions required in order to be valid (e.g., information obligations).

The Bill does not formally state that Third-Party Funding is allowed, consequently, it does not contain any more specific regulation of Third-Party Funding dealing with issues that might arise under Third-Party Funding arrangements (e.g., confidentiality and conflicts issues). For this reason, the application of Third-Party Funding will likely be, at least initially, uncertain.

VIII. COMPARISON OF THE ANALYZED COMMON LAW JURISDICTIONS APPROACHES

As seen from the above analysis, the position of most jurisdictions analyzed is to continue fully applying the doctrines of champerty and maintenance in litigation proceedings. However, especially in South Africa and England, the case law is trying to relax its application when this is necessary for the right of access to justice.

However, similarities and differences are evident in the approaches used in regulating Third-Party Funding in arbitration proceedings: England and South Africa have not enacted any new legislation. Third-Party Funding is regulated by the founders themselves in England, and by the main arbitration institution in South Africa. Both types of rules, however, are not equivalent to a legislative act. This could raise problems in terms of enforceability and uniformity in applying Third-Party Funding rules in proceedings seated in England/South Africa. Moreover, internal regulation of an arbitration institution or founders could be a great solution in terms of speedy regulating Third-Party Funding, but at the same time, it may not be sufficient to oust the doctrines of maintenance and champerty, which are principles of common law. In addition, these types of approaches do not require prerequisites for funders (e.g., minimal capital) as requested in the

other jurisdictions where Third-Party Funding is legally regulated. This may create protection problems for parties involved in a proceeding.

While Hong Kong and Singapore explicitly legalized Third-Party Funding in arbitrations,[132] Nigeria reached this conclusion through an indirect reasoning. The Nigerian Bill does not explicitly state that Third-Party Funding is legal. As a result, it may be argued that ambiguity remains and it could only be properly addressed through formal reform to applicable Federal Law.[133] As previously said,[134] common law doctrines apply in Nigeria unless they are expressly abolished or modified by legislation or case law. Since the interpretation of the new provisions is ambiguous and the legislation does not explicitly allow Third-Party Funding, courts will have to decide, once given the opportunity, whether these provisions are sufficient to oust the old doctrines of champerty and maintenance in order to permit funding agreements in arbitration.[135]

In conclusion, as seen above, all analyzed common law jurisdictions have legalized conditional fees except Nigeria. In contrast, however, South Africa allows also contingency fees. Thus, it is evident how national legal systems are moving to more and more openness towards a narrower application of the old doctrines of champerty and maintenance doctrines.

IX. CONCLUSION: POTENTIAL INSIGHTS FOR KENYA FROM THE OTHER STATES' ACTIONS

[132] For the analysis of the different approaches, see above Chapter 3, V

[133] Wheal, R., Oger-Gross, E., Obamuroh, T. and Lexner, G., 2018. *Third Party Funding in Arbitration: Reforms in Nigeria*. Whitecase.com. <https://www.whitecase.com/publications/alert/third-party-funding-arbitration-reforms-nigeria>

[134] See Chapter 4, VI, (a)

[135] Oyesanya, O., 2021. *Should Nigeria Legalise Third-Party Funding for Arbitrations? Prospects and Issues*

As seen before from the consequences of the legislative reform in Hong Kong and Singapore, benefits relating to the attractiveness of the jurisdictions as international arbitration hubs and thereby also in regard of the attractiveness for foreign investors can be observed. Since the legal availability of funding is an important consideration for parties, the availability of Third-Party Funding certainly affects the decision of parties when choosing the seat of arbitration. The presence of funders in both jurisdictions will certainly increase.

An important aspect to underline is the importance of clear regulation concerning Third-Party Funding as in Singapore and Hong Kong. The Nigerian proposal could raise problems in terms of efficacy and practice of Third-Party Funding arrangements since the legislation is not well-defined. An ambiguous regulation could lead to legal uncertainty problems. Legal uncertainty reduces the attractiveness of entering the market to funders because the funders will be unsure about the enforceability of their funding agreements in the respective jurisdiction.

As seen in the South-African approach, another way to regulate Third-Party Funding is through arbitral rules issued by arbitration institutions. This approach might be possible when legislative reforms are unnecessary (or required a complex legislative procedure) and/or when Third-Party Funding is only contemplated for international arbitration, which is mostly managed independently of legislation.

In any case, effectively regulating Third-Party Funding for arbitration would lead Kenya to become a major attraction as a seat of arbitration in the whole of Africa.

CHAPTER 4

THE BENEFITS AND RISKS OF THIRD-PARTY FUNDING FOR ARBITRATION

I. INTRODUCTION

"Third-Party Funding is a feature of modern litigation." These opening words of the judgment of the English Court of Appeal in Excalibur reflected the reality that, over the last 20 years, the role of Third-Party Funding in major litigation has become pervasive in many jurisdictions and in international arbitration.

It has in fact become increasingly popular in both international commercial and investment arbitrations as parties are seeking financial assistance and access to arbitral justice.[136] Because international arbitration cases generally involve high legal costs, a party's ability to bring a claim and prevail may be restricted by the availability of funds.

A Third-Party Funder can then play a key role in financing the claim, by easing the burden of the Funded Party while generating profit for itself.

Although Third-Party Funding has considerable advantages, which includes increasing access to justice, it also carries risks and uncertainties that this chapter will discuss.

Kenya has known a rise of cases in commercial arbitration due to influx of foreign investments and is likely to be concerned by Third-Party Funding, as any other State welcoming arbitration. The assessment of these advantages and risks can help deciding whether regulating Third-Party Funding would be interesting for Kenya.

[136] William Stone, "Third Party Funding in International Arbitration: A Case for Mandatory Disclosure" (2015) 17 Asian Disp Rev. 69

II. POTENTIAL BENEFITS OF THIRD-PARTY FUNDING FOR ARBITRATION

This section reviews the potential benefits of clarifying the position of Kenya about Third-Party Funding.

(a) Benefits to the parties of arbitration disputes in Kenya

1. Facilitating the access to justice and assessing the merits of a claim

One potential benefit of allowing Third-Party Funding in arbitration is that it may facilitate access to justice.[137] Lawyers and funders generally agree that litigation finance enables parties who may not have sufficient financial resources to pursue their legal rights and claims through arbitration.[138]

A Third-Party Funding agreement permits to the Funded Party mitigating the risk of conducting arbitration proceedings. The transfers of some or all the risk allows to the Funded Party to either achieve a successful recovery in arbitration without cost of legal fees or other, or to bear the consequences of a claim should it fail.

The importance of this consideration was emphasized when relaxing the doctrine of maintenance and champerty in Australia[139] and England,[140] but also in Hong Kong and Singapore more recently;[141] doctrines that may still apply in Kenya.

If Third-Party Funding is permitted in Kenya, funders may also want to fund cases arising before Kenyan courts. That would be a real access to justice issue. Caution should be taken with regards to litigation funding. This is a

[137] Although, the idea is disputed in the investment context, see after Chapter 5, III.
[138] Bloomberg Law's 2021 Litigation Finance Survey
[139] In *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* (2006) 229 CLR 386
[140] In *Gulf Azov Shipping Co Ltd v Idisi* [2004] EWCA Civ 292 (CA)
[141] See below, Chapter 4

separate issue that is not deal with in the report. If Kenya chooses to permit Third-Party Funding in relation to commercial arbitration, it doesn't mean that it would also be permitted in national courts. This should however be explicitly stated for greater clarification.

The Funder' due diligence conducted against its own investment criteria and the regular monitoring of the case management helps giving parties an objective view of the merits of their claim. They will receive the assistance of experts of dispute resolution in preparing and conducting arbitration and the TP Funder will bring independent, commercial and objective perspective. Such assistance can only be profitable to Funded Parties.[142]

This assistance would consist in an assessment of the strengths and weaknesses of the claim:

- The analysis of legal/factual arguments in claimant's knowledge;
- The quantum claim//likely costs and risk of pursuing claims (balance cost of claim and likely recovery);
- The terms of arbitration agreement or applicable treaty;
- The examination of arbitral institution and composition of tribunal;
- The seat of arbitration and law of arbitration agreement;
- The substantive law of the agreement;
- The potential jurisdictional issues, possible counterclaims;
- The likely timing of resolution of claim; and
- The risks associated with enforcing and obtaining payment under award.

The existence of a TPF agreement may also increase the chances of a beneficial settlement for the claimant. The knowledge of the existence of a Third-Party Funding agreement by the defendant can accelerate the resolution of the dispute. The respondent may be willing to save time and expenses; he may understand that the prolongation of the proceedings is

[142] The Law Reform Commission of Hong Kong, *Third-Party Funding for Arbitration* (Report, 2016)

not a good strategy. Indeed, not only the claimant is able to afford it, but if he received financial support of a Funder, his claim is likely to be strong.

Concerning the funding of a respondent party, Third-Party Funding could also give the possibility to assist resource-poor respondents facing several claims when they have meritorious counterclaim or as form of insurance against costs of defending their claim. The respondent party would still need to meet investment criteria of TP funders in order to receive a funding. This funding may be used as a hedge against loss in case of unfavorable award, to minimize and to predict arbitration costs, and to eliminate the effect of having uncertain litigation or arbitration on company's books in respect of the company's ability to engage in big transactions.[143]

2. Third-Party Funding in the aftermath of the Covid crisis

Third-Party Funding may be a solution to consider in the aftermath of the Pandemic.

The economic shock of the Covid-19 pandemic is profound and its impact has been felt by the whole world. Shortage in cash liquidity and increase in precautionary savings are likely to increase. Solvent companies, even those originally paying their own legal expenses, have begun seeking external financing for claims to save money. Third-Party-Funding could be an effective means for financing legal disputes after the pandemic.[144]

Small businesses' budgets have been strongly impacted by the Covid-19 crisis and large corporations are now more reluctant to spend in an uncertain economic context. An option to fashion corporations' litigation strategy is thus hedging litigation risks and taking on dispute financing. Arbitration financing is becoming an urgent trend.[145] Third-Party Funding is

[143] Maya Steinitz, *Whose Claim is This Anyway? Third-Party Litigation Funding* (Legal Studies Research Paper No 11-31, University of Iowa, 2011), p1311

[144] A. Okubote, Arbitration Finance in the Aftermath of a Pandemic: Third-Party Funding as the Magic Bullet (2021) The American Review of International Arbitration

[145] ibid

a very attractive claim funding option because of its non-recourse nature. It has in fact become an almost unavoidable commercial reality and a solution to the liquidity issues implicated by financing a claim in the aftermath of the pandemic.

(b) Benefits to Kenya

In addition to benefits to individual parties, Third-Party Funding may also hold benefits for Kenya.

1. Promoting arbitration in Kenya

Arbitration as an alternative dispute resolution method has the advantage of its flexibility, its party-controlled procedure and a greater choice over who decides a claim, the confidentiality of its proceedings and the potential for a quick and cost-efficient resolution of disputes, that may be enforced in multiple jurisdictions.

Following the adoption of a new Constitution in Kenya in 2010, its implementation has seen significant improvements in the promotion and protection of access to justice. Only 10% of Kenyans choose courts as a way of solving their legal problems. A majority prefer other modes of dispute resolution, including arbitration.[146]

Third-Party Funding may greatly contribute to the use of arbitration in Kenya. While uncertainty or prohibition of Third-Party Funding may deter international parties from selecting Kenya as a seat of arbitration; the clarification of its status as permitted would be a signal that Kenya is an arbitration friendly jurisdiction, cognizant of modern best practices. This is the biggest advantage of the recognition of Third-Party Funding in Kenya.

Third-Party Funding may as a result increase the use of arbitration in Kenya which would beneficiate to its reputation as a seat of arbitration, its

[146] HIIL, Justice Needs and Satisfaction Kenya (Report, 2017)

commitment to rule of law, its attractiveness to new investments.[147] The law of arbitration recognizes the role of the court in arbitration, but limit court intervention in arbitration to a basic minimum.[148] This should subsequently increase the confidence of foreigners in the Kenyan arbitration system. Effective and reliable application of international commercial arbitration in Africa has the capacity to encourage investors to carry on business with confidence knowing their disputes will be properly settled. This will not only enhance international commercial arbitration in Kenya but also economic development for the country.[149]

Making arbitration more easily available may also benefit the Kenyan legal system by reducing the number of commercial cases before Kenyan courts. They would have more time and resources to focus on matter from which public can better benefit. Relying more frequently on arbitration would enhance the efficiency of the Kenyan legal system. Alternative dispute resolution assists Kenya by helping judicial case load. As an example, in April 2016, more than Ksh 6.5 million worth of assets were released on successful conclusion of the mediation of a case which had been in court for 15 years. Providing examples of how helpful arbitration is difficult due to the confidentiality that surrounds this mechanism of dispute resolution. However, efforts have been made to fast track the arbitration process. It is promising to know that the latest World Bank report ranked Kenya as 61 amongst 190 economies where the preferred mode of dispute resolution is arbitration. This is a real improvement in the 15 past years.[150]

2. Increasing Kenya's competitiveness

Regulation and permission of Third-Party Funding seems to impose itself as a global trend. The concept has started to move away from dusty doctrines

[147] The Law Reform Commission of Hong Kong, *Third-Party Funding for Arbitration* (Report, 2016)
[148] K. Muiga, Settling Disputes Through Arbitration in Kenya (Glenwood Publishers, 2012)
[149] K. Muiga, Promoting International Commercial Arbitration in Africa (Paper, 2013)
[150] ibid

of maintenance and champerty; it is from now on accepted in several jurisdictions where those concepts were an obstacle, as it has been discussed earlier.[151] It is thus becoming a recognized and established option for disputing parties. Legal reforms to accomodate Third-Party Funding would make Kenyan law consistent with other regulations over the world that permit Third-Party Funding.

If Kenya chooses to clarify the status of Third-Party Funding and to permit it, a further step could be also taken in relation to investment arbitration. ICSID rules have recently expressly aknowledged Third-Party Funding. As a result, Kenyan prohibitions in relation to investment arbitration would have no legal effect. Permitting Third-Party Funding in investment arbitration may have some benefits for Kenya as well, but they will not be discussed in the report which is focused on commercial arbitration.

Concerning the Kenyan arbitration environment, as discussed earlier in the report,[152] there has been a rise of arbitration to resolve commercial disputes due to influx of foreign investments.

In view of this recent evolution of the concept of Third-Party Funding, Kenya's competitiveness may be promoted if Kenyan law made it clear that it permits Third Party Funding for arbitration. If the capacity to handle international and domestic arbitration is exploited at its maximum, it may be a possibility to prominently place Kenya on the global map of international arbitration.

There is a need to employ mechanisms that will help promote and demonstrate Africa to the outside world as a place endowed with international commercial arbitrators with sufficient knowledge and expertise to be appointed to arbitrate international arbitrators. This would not only afford the local international commercial arbitrators the fora to showcase

[151] See below Chapter 4
[152] See below Chapter 3

their skills and expertise in international commercial arbitration but may also attract international clients from outside Kenya.

III. POTENTIAL RISKS OF THIRD-PARTY FUNDING FOR ARBITRATION

Although formally addressing and regulating Third-Party Funding may have some significant advantages, the risks and concerns regarding Third-Party Funding also require evaluation.

(a) Promotion of unnecessary arbitration proceedings

Lawyers and Funders disagree about whether litigation finance enables more frivolous lawsuits.[153] Third-Party Funders argument is that they would only fund cases meeting their investment criteria (that is to say, claims with reasonable chance of success), as a consequence it would be unlikely that Third-Party Funding would increase the number of frivolous claims. The reasoning can be illustrated by the example of another jurisdiction which allows Third-Party Funding. It has been shown in Australia that the legal experience, expertise and risk aversion of Third-Party Funders in commercial litigation prevents unmeritorious claims.[154]

On another side, funders have only a monetary interest in arbitration cases. They may consider funding cases, even frivolous, if they find a financial interest in doing so. Moreover, it has to be recognized that assessing a case is a very delicate and difficult operation. The assessment provided by the legal experts advising funders is not an exact science and some circumstances or facts can lead to unexpected and unforeseeable outcomes.

(b) Ethical concerns

[153] Bloomberg Law's 2021 Litigation Finance Survey

[154] Justice for Profit: A Comparative Analysis of Australian, Canadian and US Third-Party Litigation Funding" (2013) 61(1) *American Journal of Comparative Law* 93, at 142

Some ethical concerns arise in relation to Third-Party Funding. The question is whether commodification of cases should be permitted and whether non-parties to a dispute should be authorized to make profit from the arbitration system. Funding could provide access to justice to the most vulnerable and make the arbitration system more efficient. It has to be considered whether the benefits outweigh the demerits.

(c) Third-party control and influence

One must keep in mind that the primary interest of funders is generally a monetary one.[155] Third-Party Funders bear the financial risk of arbitration and costs of legal representation. As a consequence, they may want to interfere in the claim funded when it comes to the choice of counsel and the decisions on legal strategy.

The conduct of Third-Party Funders in relation to case management could however be addressed by the law in the preferred direction. In fact, while the Australian law permits a high degree of control of the Third-Party Funder over a funded case; English courts want the Funded party to retain control over his claim.

Additionally, despite the scope of control given to Funders by the funding agreement, legal representatives have professional and ethical duties, and responsibilities to the funded party (and not to the funders). They are not supposed to act in the commercial interests of the funders if they conflict with duties to funded party.

The existence of Third-Party Funding may also impact the social function of justice. The availability of funding for a respondent could lead to a corporate-defense quasi-immunity. Indeed, if corporations feel protected from the impact of (punitive) damages thanks to the transfer of risk to their

[155] Although there has been a development of non-profit funders recently, but they won't be considered in this report.

Third-Party Funders, there may be less deterrence and incentive to not engage in harmful activities.[156]

To counteract this potential impact of funding respondents, the Third-Party Funding scope of use could be limited to commercial and business disputes. The proposition is however to be deeply considered and examined.

(d) Costs of Third-Party Funding and recoverability; security for costs and liability for adverse costs

The sub-section considers the consequences of the absence of regulation of the structure of the Third-Party Funding agreement and how recoverability of costs can be a concern. It also highlights some issues in relation to liability for adverse costs awards or orders, as well as security for costs.

1. The structure of the Third-Party Funding agreement and the recoverability of Third-Party Funding costs

There are no standards concerning the terms and how Third-Party Funding is to be provided. There is no regulation either concerning the return or percentage to which Third-Party Funders are entitled.

This lack of standards may result in an imbalanced bargaining power of the parties to the funding agreement. The Funded Party could agree to unfair and unreasonable terms. As a consequence, the Funded Party may run the risk of excessive costs of Third-Party Funding (the proportion of awarded amounts entitled to Third-Party Funders).[157]

A Funding agreement will require the Funded Party to reimburse the Third-Party Funder with a percentage of the recovery. A successful Funded Party

[156] Maya Steinitz, *Whose Claim is This Anyway? Third-Party Litigation Funding* (Legal Studies Research Paper No 11-31, University of Iowa, 2011), p1312
[157] The Law Reform Commission of Hong Kong, *Third Party Funding for Arbitration* (Report, 2016)

may attempt to recover funding costs from the other party as part of the costs allocation exercised at the end of the arbitration.

The concern lies in the question of whether an arbitrator can and should allocate funding costs. The ICCA-QMUL Report suggests that any legal costs that the funded party is contractually obliged to repay to the Third-Party Funder should be considered as legal costs incurred by the Funded Party. Where recovery of costs is limited to incurred costs, the obligation on the successful Funded Party to reimburse the Funder would be sufficient for a tribunal to find that the party's costs fall within that limitation. Whether the costs of funding are recoverable depends on national legislation and procedural rules and should be subject to a test of reasonableness. The test should include on the following and non-conclusive list of factors: whether the respondent's conduct has caused the impecuniosity of the claimant, whether the claimant had no other option but to seek funding from a Third-Party Funder to pursue its claim, and whether the respondent had knowledge that the claimant received Funding.

2. Liability for adverse costs awards or orders

An arbitral tribunal at the end of the proceedings decides on how costs incurred by the parties have to be apportioned between them. These costs reward or punish a party for its conduct and so recognize whether the claimant had a meritorious claim in arbitration.

Adverse costs awards can be made where the claim is legally unsound, without merit, or where the quantum claim is overstated (costs the respondent had to handle in defending his position were unnecessary). In the later situation, the arbitral tribunal can sanction the claimant by ordering him to pay for those costs. The potential allocation of costs raises questions about what happens with respect to legal costs when a Third-Party Funder is involved.

In the litigation context, courts in England[158] and in the United States[159] have ruled that costs could be awarded against the Funder if he obtained a sufficient degree of economic interest and control in relation to the funded claim. The idea behind these rulings is that funders would financially benefit from a successful claim, so they should not be exempted from responsibility for adverse costs if the Funded Party loses.

However, a tribunal in the context of international arbitration will not generally be able to make an adverse costs order directly against the Third-Party Funder since it is not a party to the arbitration agreement. The basis on which the tribunal would make that order is unclear. Unless Third-Party Funders become parties to the arbitration agreement, orders against them would be unenforceable. The risk is thus that some costs may go unpaid when there is a Funder. This risk is increased because arbitral tribunals do not have power over the funder.

The revised *IBA Guidelines on Conflicts of Interest* states that a Third-Party Funder 'bears the identity' of the funded party to the arbitration. It is however unclear whether the concept extends the jurisdiction of the arbitral tribunal to include Third-Party Funders in the context of adverse costs. Consent to be part of an arbitration agreement is a requirement of essence.[160] The test for considering a non-signatory as party in the arbitration is demanding, and courts generally recognize that there is a presumption that only signatory parties should be the parties in an arbitration, and thus subject to a tribunal jurisdiction.[161]

However, it would be fair for a Third-Party Funder who can highly benefit from a successful claim to be also liable for adverse costs in the event the

[158] *Excalibur Ventures LLC v. Texas Keystone Inc & Ors* [2016] EWCA Civ 1144
[159] *Mohammed Abu-Ghazaleh et al. v. Gerard Martin Demerutis Chaul et al*, Florida Third District Court of Appeal, (Nos. 3D07–3128, 3D07–3130) Decision of 2 December 2009, 36 So. 3d 691
[160] Article II, The Convention on the Recognition and Enforcement of Foreign Arbitral Awards
[161] ICCA-QMUL Report on Third-Party Funding in International Arbitration

Funded Party loses, the same way it is in litigation.[162] If Third-Party Funder are confident in their investment, they should not be worried about the potential liability.

For these reasons, a Third-Party Funder may be liable for costs awarded against a Funded Party, or at least for costs which are awarded as a consequence of the outcome of a case.[163] They may however not be liable for any costs incurred as a result of the Funded Party's conduct in the arbitration, especially in cases where Funders exercise a limited control over the conduct of the Funded Party and its counsel. Another proposition would be to give tribunals the power to directly award costs against funders. This could be addressed by binding rules in national law or arbitration rules.

3. Security for costs

Security for costs is a special type of interim measure requested by the respondent of a claim or counterclaim to address situations in which the claimant may be unable to pay the adverse costs award rendered against him.[164]

Third-Party Funding may imply the impecuniosity of the claimant and could be a reason for awarding security for costs. But the question is left open to tribunals of whether security for costs should be provided easily to the respondent as it may cause difficulties in achieving arbitral justice. Before a tribunal grants an application for security of costs, they may want to consider whether there is enough proof that the current financial situation of the funded party will result in the non-payment of the requesting party's costs at the end of the proceedings.[165] A tribunal should base its decision on the existence of the funding agreement, but also on the financial records of the funded party as a whole. If the funded party has evidence that the

[162] Hong Kong Law Reform Commission's Final Consultation Paper (2015)
[163] Hong Kong Law Reform Commission's Final Consultation Paper (2015)
[164] J. Goeler, *Third-Party Funding in International Arbitration and its Impact on Procedure* (Kluwer 2016)
[165] J. Waincymer, *Procedure and Evidence in International Arbitration* (Kluwer 2012)

funder will cover adverse costs or that it has itself sufficient financial means, orders granting security for costs would thus not be necessary. In fact, the existence of a Third-Party Funding Agreement should not in itself suggest that the Funded Party is impecunious; following the Covid-19 crisis, even large corporations usually financing their own legal costs started to rely more importantly on arbitration funding.[166]

Third-Party Funding may also hinder the respondent in achieving their desired justice since the costs would be paid by the Third-Party Funding and not the insolvent claimant. It may prevent the right to compensation of the respondent if security for costs is not ordered.

(e) Potential for breaches of legal professional privilege and confidentiality issues

Another potential risk with Third-Party Funding is that is raises concerns about protection of client confidentialities. The purpose of attorneys' obligations of confidentiality and the doctrine of legal privilege is to allow transparent communications between lawyers and clients without concerns about disclosure of those communications to other parties in litigation or arbitration.

The involvement of an additional entity in the assessment of the merits of a claim can lead to questions about the application of privilege. The impact of Third-Party Funding on privilege remains an area with uncertainty, in particular when communicating with and providing documents to a Third-Party Funder.

Before deciding to fund a claim, a Funder will usually conduct comprehensive due diligence to evaluate the chances of success of the case

[166] A. Okubote, 'Arbitration Finance in the Aftermath of a Pandemic: Third Party Funding as the Magic Bullet' (2021) The American Review of International Arbitration

to be funded. Third-Party Funders may also require a regular review and monitoring of the management of the funded claim.

The Funded Party may thus be asked to provide information and documents to the Funder.

The question of whether a party who discloses privileged documents or communication to a Third-Party Funder in order to secure funding risks waiving privilege is really challenging in the context of international arbitration. The complexity stems from the broad discretion afforded to tribunals to determine evidential matters of their own accord, the lack of any substantive privilege rules in any institutional rules or arbitration legislation, and the considerable legal and conceptual differences in privilege rules across jurisdictions.

In Kenya, privilege is regulated by the Evidence Act and Common Law. Communications between a lawyer and their client are strictly protected by the Section 137 of the Evidence Act. Communications with in-house lawyers and external legal advisers who are advocates are also privileged.

Section 134 of the Evidence Act is categorical that no advocates shall at any time be permitted, unless with his client's express consent, to disclose any communication made to him in the course and for the purpose of his employment, unless a crime or fraud has been committed in relation to the case.

Communications with Third parties are not protected, except communications related to medical records and spousal communications. As a result, some communications between a Funded Party's legal counsel and a Third-Party Funder are not protected by the legal professional privilege.

Communications by a counsel to the Third-Party Funder and the Funded Party concerning arbitration are not covered. However, this kind of

communication could be covered by the litigation privilege, which protects any document or communication created for the primary purpose of preparing litigation between a client, a lawyer or a Third party.

Communications by counsel to the Funded Party, that the latter would then transmit to the Third-Party Funder are not protected either. Indeed, the transmission of communication may constitute an implied waiver of the legal professional privilege by the Funded Party itself.

As a consequence, these communications may be object of disclosure requests in the arbitration proceedings or related national courts proceedings.[167]

This risk of disclosure has led to a consensus amongst Third-Party funders that due diligence on a claim should focus on facts available, rather than legal opinions being transferred.[168]

The ICCA report proposes useful principles that may be applied in the context of Third-Party Funding. Whilst the existence of Third-Party Funding and the identity of the funder are not legally privileged, some information in the funding agreement is likely to be legally privileged and the production of such information should not be ordered. Tribunals should not treat any privilege as waived solely because it was provided to a Third-Party Funder for the purposes of the funding relationship. Tribunals should also permit to be redacted the funding agreement or other information provided to a funder which is otherwise disclosable.

[167] ICCA-QMUL Report on Third-Party Funding in International Arbitration

[168] Maxi Scherer and Aren Goldsmith, 'Third Party Funding in International Arbitration in Europe: Part 1 Funders' Perspectives' (2012) (2) 2012 *International Business Law Journal* 207, at 216

The law on privilege has not been harmonized on an international level and varies significantly between jurisdictions. This leaves the position somewhat unclear on communications with Third-Party Funders.

An added complexity is that there is no established consensus on how to determine which national rules should apply. Tribunals often determine it through a complex conflict of laws analysis, by applying the 'closest connection' test or by applying a 'most favored nation' approach. Absent an agreement in the arbitration agreement itself regarding the scope of discovery, the parties will thus need to consider carefully which countries' privilege laws might be applicable and how they might apply to communications with funders.

An option if Kenya were to affirmatively regulate Third-Party Funding would thus be to rely on the concept of party autonomy. Parties may consider drafting confidentiality agreements between the parties and the Arbitrator, setting out the matters covered therein and the extent of the said confidentiality. They may decide that, provided by agreement, without consent of parties, only such information as required by law shall be disclosed in connection with enforcement or challenge.[169]

(f) Disclosure of Third-Party Funding agreement and conflicts of interest

The disclosure of Third-Party Funding agreement is a thorny debate at the heart of the discussion concerning the possible regulation of Third-Party Funding. A disclosure would consist in an acknowledgment by a party in arbitration that it has been funded by a Third Party. The debate centers around different questions: whether such a disclosure should be mandatory; if so, at which time of the procedure it should occur; and whether only the identity of the Third-Party Funding or the entire agreement

[169] Claude R.Thomson & Annie M.K Finn, "Confidentiality in Arbitration; A valid Assumption? A proposed solution! "(2007) Dispute Resolution Journal Vol. 62.No 2

should be disclosed. At the moment, there is no general and mandatory rule requiring parties to disclose Third-Party Funding agreements.

Permitting Third-Party Funding may also create new conflicts of interest between the legal professionals involved in the arbitration process. Legal counsel and arbitrators may face new situations of conflicts of interest that they would have to disclose.

1. Disclosure of Third-Party Funding agreement

Knowledge by the adverse party of the existence of a Third-Party Funding agreement may significantly affect its conduct regarding the settlement of the claim. This other party can adapt its strategy to either try to undermine the relationship between the Funded Party and its funder or moving towards a settlement of the claim to save time and expenses.

The disclosure of Third-Party Funding may unduly influence the arbitral tribunal and prevent the proper settlement of a case.

The disclosure of the existence of a Third-Party Funding agreement and of the identity of the Funder should be systematic to ensure that any possible conflicts are uncovered as early as possible in the process.

2. Disclosure of conflicts of interest

Arbitrators have a duty to disclose potential conflicts of interest. They must inform the parties of any circumstances that could give rise to doubts over their impartiality or independence. This obligation is ongoing for the entire duration of the arbitration.

With the increase of the use of Third-Party Funding, new sources of conflict of interests for the legal professionals involved in the arbitration arise.

Concerning the legal counsel of a party, a conflict may arise if a Third-Party Funder frequently funds the same law firm (albeit for different clients). The

conflict may come from the economic reliance of the law firm on the Third-Party Funder and its duties towards its clients. A conflict may also arise during the settlement of negotiations. It may be in the financial interest of the Third-Party Funder, and of the law firm, to settle or not to settle a claim. However, this financial interest may conflict with the law firm's client best interests.

Concerning the arbitrators, a conflict may arise when an arbitrator is appointed frequently by a party funded by the same Third-Party Funder. It is to the arbitrator to consider whether it affects his impartiality. This frequent choice of the same arbitrator, and the potential impartiality resulting from, can also be the basis of a challenge to his appointment.

The IBA guidelines on Conflicts on Interest in International Arbitration may require disclosure of Third-Party Funding. Article 7 stipulates that when a Third Party has direct economic interests with the outcome of the award, or bears the liability for compensation to the other party, if the arbitrator has a direct or indirect relationship with the Third Party, it should be notified and disclosed to the arbitral tribunal, the other party and the arbitral institution. However, these Guidelines are not mandatory, and may not apply to all Funding Agreements.[170]

If Kenya decides to formally legalize and regulate Third-Party Funding, the risk is that of an increase of conflicts of interests before and during the arbitration process. Client's best interests may be disregarded, and arbitrators challenged for new reasons.

The systematic disclosure of the existence of a Third-Party Funding agreement would considerably decrease the chance of a challenge based on the arbitrator's lack of impartiality and independence, including at the time of the enforcement of an arbitral award before national courts.

[170] ICCA-QMUL Report on Third-Party Funding in International Arbitration

The Third-Party Funding disclosure system is likely to be on the agenda of the arbitration institutions in the coming years. The Nairobi Centre for International Arbitration may then be interested in looking deeper at the matter. As an example, the New 2021 ICC Rules of Arbitration, which came into force on 1 January 2021, explicitly refer to Third-Party Funding and include at Article 11(7) the new requirement for parties to disclose any Third-Party Funding agreements so that potential conflicts of interests are identified and managed.

(g) Risk of arbitrary termination of the Third-Party Funding agreement

Despite its popularity and potential utility, Third-Party Funding also comes with concerns such as when and on what basis a Funder may terminate its funding to a party. During the negotiation of the scope of the withdrawal of funding by a Third-Party Funder, the competing interests of both the Funded Party and the Funder have to be considered.

A Funded Party has entered into such an agreement because he may need a financial support. Third-Party Funding agreements include termination clauses. These clauses should detail the situations where the Funder may terminate the agreement and the obligations that should survive this termination. A scope which would be too broad concerning the power of withdrawal of a Funder would create an imbalanced relationship between the parties to the Third-Party Funding agreement. The Funded Party may be under indirect influence of the Third-Party Funder when conducting the arbitration so as to ensure this continuous financial support.

(h) Insufficient Third-Party Funder capital adequacy

An insufficient Third-Party Funder’s capital adequacy can also become a concern.

The capital adequacy is the ratio of the Third-Party Funder's capital to its assets (the funding arrangements). A minimum level of capital is essential to protect the Third-Party Funder against unexpected losses in the event the funded claim does not succeed, but also to gain the confidence of the Funded Party as to the financial ability and sustainability of the Third-Party Funder which pays for the often substantial costs of arbitration.[171]

Considering the importance of this capital adequacy to the Funded Party, it has been considered that this factor should be regulated by a statutory body, as it has been suggested in the UK with the Financial Services Authority.[172]

(i) ***Inadequate complaints procedure***

Another risk to consider is that inadequate complaints procedure can give limited recourse to aggrieved funded parties.

There do not appear to be any formal procedures or rules to deal with complaints against the potential conduct of Third-Party Funders in Kenya. Those procedures and rules are of essence to adequately protect Funded Party from being exploited by Third Party Funders, and to deter the later to engage in inappropriate conduct.

(j)Money laundering

The risk of money laundering is part of any activity involving money or financial services. Some people argue that Third-Party Funding in arbitration may be used as a mean to launder the monetary proceeds of criminal activity. Money launderers could seek to disguise the source of funds by having payments made by or to associates or Third parties. Certain States specifically link transparency requirement in the context of Third-Party litigation funding to anti-money laundering, demonstrating that such

[171] Lord Justice Jackson*, Review of Civil Litigation Costs*, Final Report (2009), at 121
[172] ibid

schemes can be used for money laundering purposes.[173] The same could be done in relation to arbitration funding.

IV. CONCLUSION

This chapter had the purpose of scrutinizing the opportunities and risks of clarifying the position of Kenya on Third-Party Funding.

Whether the benefits outweigh the risks is one of the main questions leading the debate concerning the status of Third-Party Funding in Kenya.

Third-Party Funding would bring a number of advantages for arbitration in Kenya, if it were to permit it in national arbitration. It would especially keep Kenya in the line of what other jurisdictions such as Singapore have done recently. The main advantage of permitting Third-Party Funding is clearly that of signaling Kenya as an arbitration-friendly jurisdiction that is cognizant of modern best practices; while prohibitions may deter international parties to choose Kenya as a seat of arbitration. If Kenya were to permit Third-Party Funding in relation to arbitration, it may want to extend Third-Party Funding directly to court cases in the Kenyan legal system. This is a matter to specifically scrutinize and clarify.

The risks accompanying Third-Party Funding have also been discussed: the potential unnecessary proceedings, the possibility for Third-Party funders to control and influence the case, the questions arising in relation to costs of Third-Party Funding and recoverability, security for costs and liability for adverse costs. Third-Party Funding may lead to the breach of legal professional privilege and confidentiality. New conflicts of interests may also arise and nourish the debate surrounding the disclosure of Third-Party Funding agreement. In order to properly assess these risks, the question to

[173] Luxemburg's Law on Alternative Investment Fund Managers of 12 July 2013

be asked is whether they could be adequately addressed and managed by new safeguards.

CHAPTER 5

RECOMMENDATIONS

I. CONSIDERATIONS

For our final recommendations we have considered Kenya's current status and its ambitions regarding its potential future position as arbitration center. In this context, we have considered its current and potential position in relation to other African countries but also in a global context. We have further taken into account other states' legislative actions in regard of Third-Party Funding and its consequences for the respective arbitration hubs.

In light of the above-mentioned considerations and chapters 1 to 4 of this White-Paper Report we have come up with the following recommendations.

II. RECOMMENDATION 1 – LEGISLATIVE ACTION CONCERNING THIRD-PARTY FUNDING

Concerning the main question of this White-Paper Report being the need of legislative action concerning Third-Party Funding in Kenya, we are of the following opinion.

We have concluded that Kenya's competitiveness as an international arbitration centre will likely be reduced if the law is not clarified to make it clear that Third Party Funding for arbitration taking place in Kenya is permitted. As elaborated in Chapter 2 III (e), the practical consequences of not expressly regulating Third-Party Funding might be marginal in light of the options the parties of the funding agreement have to avoid a potential invalidity of the funding agreement. Also, the chances of the arbitral award being affected regarding its enforceability or the risk of set aside can be

considered low. Nevertheless, the remaining ambiguity might still lead to investors being hesitant to enter the market in Kenya.

This can be evidenced with the consequences of the legislative reform in Hong Kong and Singapore, which benefitted from expressly regulating Third-Party Funding in their jurisdictions.

We consider from our review of the law in Kenya (Chapter 2) and other jurisdiction that there are benefits to the stakeholders in arbitration when regulating Third-Party Funding. We are also of the view that the potential risks arising from Third-Party Funding are manageable by implementing clear ethical and financial standards which will provide necessary safeguards. Therefore, we recommend the following:

Recommendation 1

We recommend that Kenyan laws should be amended to provide that Third-Party Funding for arbitration taking place in Kenya is permitted.

III. RECOMMENDATION 2 – ETHICAL AND FINANCIAL STANDARDS

Having clear ethical and financial standards for Third-Party Funders providing Third-Party Funding to parties to arbitration is important, not only in regard of the substantive advantages the legislative system would gain from good rules in that regard, but also in regard of the general acceptance of Third-Party Funding in Kenya.

The reviewed jurisdictions show that while Third-Party Funding for arbitration is permitted, there is little uniformity in the form of regulation of Third-Party Funding. The main trend is toward a light touch approach either by including statutory regulation of financial conflicts issues or self-regulation such as in England and South Africa.

We consider Kenya should develop its own model of regulation in regard of ethical and financial standards. For this, specific cultural and financial needs should be taken into account. Inspiration can be derived from the experience and the different approaches of other relevant jurisdictions. We recommend the following:

Recommendation 2

We recommend that clear ethical and financial standards for Third-Party Funders providing Third-Party Funding to parties to arbitrations taking place in Kenya should be developed.

IV. RECOMMENDATION 3 – DEVELOPMENT AND SUPERVISION OF APPLICABLE ETHICAL AND FINANCIAL STANDARDS

As to the question on how to regulate Third-Party Funding to a party to an arbitration taking place in Kenya, we do not have fixed views on how this should be executed. Certainly, an amendment of the Arbitration Act could be one method of incorporating rules for Third-Party Funding in Kenya. It would also be possible to develop a set of Codes of Conduct to establish ethical and financial standards for Third-Party Funders (this was done by The Association of Litigation Funders of England and Wales (**ALF**) although the Code was drafted by a Ministry of Justice Working Group consisting of representatives of various stakeholders).

Regarding a self-regulatory approach in Kenya, we consider potential challenges by contrast to England including that (i) there is no critical mass of Third-Party Funders in Kenya; and (ii) Third Party Funders are generally not incorporated in Kenya. Furthermore, public confidence might be better ensured with public laws, implemented through legislative acts of the competent authority.

The question which further needs to be tackled is whether Third-Party Funders would need to have a registered office and assets in Kenya and especially how any ethical and financial standards for Third-Party Funders should be enforced.

The following areas have been considered in other jurisdictions regarding the regulation of Third-Party Funding.

(a) Capital adequacy requirements

Sufficient minimum capital of Third-Party Funders can be considered of one of the key features when regulating Third-Party Funding. This reflects especially the public interest to ensure that Third-Party Funders are duly established and fit and proper to provide Third-Party Funding. We are of the view that Third-Party Funders should satisfy capital adequacy requirements. The requisite amount of capital can be considered in due course.

(b) Conflicts of interest

The area of conflicts of interest should be considered when regulating Third-Party Funding since it is likely that situations will arise from time to time where interest of a Third-Party Funder may conflict with the interests of the funded party and other stakeholders.

(c) Confidentiality

Confidentiality is considered as one of the biggest advantages of arbitration over court proceedings. A dilemma can arise where a Third-Party Funder requires disclosure of key facts in the proceedings to enable it to decide whether to fund a party. This is an issue for which regulation should also be considered.

(d) Privilege

It is uncertain whether communications between the Third-Party Funder and the Funded Party (and their representatives) are privileged. The operation of rules on privilege and waiver should be considered in the context of Third-Party Funding for arbitration.

(e) Control of the arbitration by Third-Party Funders

Given that Third-Party Funders are bearing the financial risk of the arbitration, they might want to exercise certain control over the arbitration funded. The nature of the control will be governed by the terms of the funding agreement to the extent permitted by the applicable law. It should be considered, how far Kenyan legislative authorities want to allow the external control of arbitral proceedings by Third-Party Funders.

(f) Disclosure

Mandatory disclosure by a party that is receiving Third-Party Funding is required in certain jurisdictions and is recommended by the *IBA Guidelines on Conflicts of Interest in International Arbitration*. It should be considered if these rules should also be adapted in Kenya when regulating Third-Party Funding.

(g) Termination of Funding

The termination of the funding agreement is likely to have serious effects for the funded party. It may lead to the funded party not being able to proceed with the arbitral proceeding. We consider that safeguards to be imposed in this regard should be explored.

(h) Liability for adverse costs

It should be further considered whether or not a Tribunal should be granted the power to make adverse costs orders against Third-Party Funders in

Kenya. An argument for establishing a possible liability of Third-Party Funders for adverse costs is that the funders would be permitted to enjoy the proceeds of a successful claim but not be liable for costs if they have funded an unmeritorious claim or breach ethical and financial standards. This does not seem justified, especially since there would potentially be no other party able to bear the adverse costs.

One approach to overcoming limitations, arising from the existing arbitral theory concerning the limitation of a Tribunal's jurisdiction in relation to third parties, would be for a Third-Party Funder to contractually submit to the Tribunal's jurisdiction on a case-by-case basis.

(i) Body issuing regulatory standards

The question arises about which statutory or governmental body should be responsible for drafting regulator standards applicable to Third-Party Funding. One possibility would be for the Department of Justice to establish a working group with representatives of the main stakeholders in arbitration in Kenya, including the NCIA, to draft a code of conduct setting out the ethical and financial standards to apply to Third Party Funding for arbitrations in Kenya. To comply with Kenyan law, a Third-Party Funder would be obligated to agree in writing with such a code of conduct when funding an arbitration taking place in Kenya. It could therefore also be helpful to invite well known and established Third-Party Funders to the working group when drafting a code of conduct.

(j) Conclusion

Concluding from the above, it is apparent that there are several issues to be dealt with when drafting ethical and financial standards for Third-Party Funding in Kenya. It is of outmost importance to have clear and acceptable rules, from both the publics' and the stakeholders' perspective, to establish effective and successful rules. We therefore recommend the following:

Recommendation 3

We recommend the establishment of a working group, possibly administered by the Department of Justice and the NCIA, to first elaborate on the question on how Third-Party Funding and especially questions regarding ethical and financial standards should be regulated.

We further recommend to address the following non-exhaustive list of potential issues when regulating ethical and financial standards:

(a) capital adequacy;

(b) conflicts of interest;

(c) confidentiality and privilege;

(d) control of the arbitration by the Third-Party Funder;

(e) disclosure of Third-Party Funding to the Tribunal and other party/parties to the arbitration;

(f) grounds for termination of Third-Party Funding;

(g) liability for adverse costs.