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By Fax No: 2840 0716

24 February 2017

Ms Sophie LAU
Clerk to the Bills Committee
Legislative Council Complex
1 Legislative Council Road
Central
Hong Kong

Dear Ms LAU,

Bills Committee on the Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Bill 2016

Government's Response to the Issues Raised by the Bills Committee at the Meeting of 14 February 2017

At the meeting of the Bills Committee of the Legislative Council held on 14 February 2017, the Government was requested to provide a written response to a list of follow-up actions (LC Paper No. CB(4)620/16-17(01)), which it subsequently received via your email of 20 February 2017. The Government's response is as follows.

(a) Solicitors' referral to third party funders

2. The common law offence of maintenance is defined as "the giving of assistance or encouragement to one of the parties to an action by a person who has neither an interest in the action nor **any other motive recognized by the law as justifying his interference**" (para 3 of the Law Commission of England and Wales (1966) *Proposals for Reform of the Law Relating to Maintenance and Champerty*, and referred to by Bokhary PJ of the Court of Final Appeal ("CFA") in *Winnie Lo v HKSAR* (2012) 15 HKCFAR 16, para 10 (emphasis added)).

3. In the earlier case of *Unruh v Seeberger* (2007) 10 HKCFAR 31, the CFA held that the fact that an arrangement may be caught by the broad definitions of maintenance or champerty is not itself sufficient to found liability. Countervailing public policies must be taken into account, especially policies in favour of ensuring access to justice and of recognizing, where appropriate, legitimate common interests of a social or commercial character in a piece of litigation (See paras 103 to 104 of the Judgment).

4. Referral to third party funding with a view to facilitating resolution of disputes by arbitration may enhance access to justice. Therefore, a solicitor's act of referral to a third party funder enabling a client to pursue a legitimate claim through arbitration in a manner recognized to be lawful under the Bill upon its commencement after enactment would not, by reason of that, amount to "maintenance".

5. The same, however, cannot be said where an extra fee is charged on top of a solicitor's professional services or a secret profit (paid by third party funders or other third parties) is made.

6. In any event, lawyers practising in Hong Kong are subject to the applicable statutory provisions and professional conduct rules concerning, in particular, the following duties: (a) to avoid conflicts of interest, (b) not to act on the basis of contingency or success fees; and (c) to observe their duty of confidentiality to the client (See paragraph 3.69 of the Consultation Paper of the Sub-committee on Third Party Funding for

Arbitration).

(b) Exclusion of persons practising law or providing legal services from third party funding

7. We have set out our the considerations as to why a person practising law or providing legal services should be excluded from third party funding for arbitration in parts (c) and (d) of our reply to Assistant Legal Advisor dated 10 February 2017. As pointed out by the Law Reform Commission ("LRC") in paragraphs 3.35 - 3.36 of the Report on Third Party Funding for Arbitration ("the LRC Report"), it is in the public interest, including that parties be represented by independent counsel focused on their service, and of maintaining the integrity of dispute resolution, that lawyers should focus on their provision of professional services to their clients and should not place themselves in a conflict of interest position by engaging in the business of third party funding. Nor does Hong Kong law currently permit Hong Kong lawyers to charge conditional and contingency fees. The identity of those providing legal services (even if not admitted as lawyers), including on the internet, is expanding, so that similar considerations apply to such providers of legal services.

8. Currently, there is uncertainty under the common law as to whether the doctrines of maintenance and champerty apply to third party funding for arbitrations taking place in Hong Kong, as appears from the judgment in *Unruh v Seeberger*[1] (above) where the CFA expressly left open this question.[2] (LRC Report paragraph 1.6)

9. The proposed legislative amendments mentioned in the LRC Report merely seek to clarify that third party funding of arbitration and associated proceedings (other than funding provided by a person practising law or providing legal services) is not prohibited by the common law doctrines of maintenance and champerty. The proposed

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[1] (2007) 10 HKCFAR 31, at paragraph 123.

[2] While earlier in *Cannonway Consultants Limited v Kenworth Engineering Ltd* [1995] 2 HKLR 475 (a decision of the High Court), it had been held that the law of champerty did not extend to arbitration, the CFA in *Unruh v Seeberger* did not refer to this aspect of the judgment .

law reform does not alter the current legal position otherwise than as stated above. As such, any persons who engage in third party funding activities not falling within the above scope would need to assess their own risks in so doing.

10. The new section 98G(2) now proposes that "third party funding of arbitration does not include the provision of arbitration funding directly or indirectly by a person practising law, or providing legal services, whether in Hong Kong or elsewhere."

11. The Government proposes the new section 98G(2) because it agrees with the recommendation of the LRC Report to exclude any funding provided either directly or indirectly by a person practising law or providing legal services from the definition of "Third Party Funding" of the Bill. The main consideration from a legal policy perspective is that a review on the existing general ban on conditional or contingency fee agreements would go far beyond the terms of reference of the LRC Report and the scope of the present legislative exercise.

12. It was noted that Hong Kong thus far had not allowed contingency fees. As pointed out by the LRC Report, the subject of conditional fees has been the subject of a separate Law Reform Commission *Report on Conditional Fees* (2007). The Government does not intend to reopen the contingency fees study at this juncture. Further discussion on the conditional fees issue now will open up complex legal policy issues and would impede the implementation of the LRC Report.

13. The Government would like to draw Members' attention to the fact that at the time when the Law Commission of England and Wales proposed the abolition of the common law offences of maintenance and champerty in its 1966 report on *Proposals for Reform of the Law Relating to Maintenance and Champerty,* it was pointed out that the question of whether solicitors should be permitted to charge their remuneration in contentious matters on a "contingency fee" basis is a big question upon which the professional bodies as well as the public must have further time for reflection before any solutions can or should be formulated (see paragraph 19). At the same time, the Law Commission of England and Wales proposed that further study, in consultation with the Law Society, should be given to the question of "contingency fee" arrangements (see

paragraph 20). The Government is of the view that similar considerations should be taken into account in Hong Kong. For the above reasons, the Government supports the conclusion of the LRC that a person practising law or providing legal services should be excluded from third party funding for arbitration and is thus of the view that the new section 98G(2) in the Bill should not be deleted.

(c) The expression of "common barrator"

14. Section 98K seeks to state clearly that particular common law offences do not apply in relation to third party funding of arbitration. The most direct and comprehensive way to achieve that purpose is to specify the offences by their names under common law rather than seeking to otherwise describe the offences in a different manner. This approach has been used for the common law offences of maintenance and champerty as well as for the less known common law offence of being a common barrator. A statutory definition is unnecessary and there is always some element of risk in defining a common law concept by legislation in a way which may not cover only the exact same scope which is subject to what the court may from time to time declare what it is in real contested cases.

15. The concepts relevant to the offence of being a common barrator have been explained in part (g) of our reply to Assistant Legal Advisor dated 10 February 2017. For instance, barratry is a subset, or an aggravated form, of maintenance, in that barratry adds frequency to the string of elements for maintenance. It is noteworthy that the same approach, i.e. citing its name under the common law, was also used in other jurisdictions when the offence of being common barrator was dealt with. See for example section 13(1)(a) of the Criminal Law Act 1967 of the United Kingdom and section 68(c) of the Law Reform (Miscellaneous Provisions) Act 1955 of the Australian Capital Territory.

(d) Power of the Advisory Body to disclose information to the public

16. In relation to the question of whether the advisory body appointed

under the new section 98W ("the Advisory body") has the power to disclose information which is received by the said body pursuant to the new section 98P to the public, it must be considered very carefully, taking into consideration the following issues.

17. In relation to information relating to any complaints made against a third party funder by a funded party received by the third party funder concerned during a reporting period and details of any findings by a court or arbitral tribunal of a third party funder's failure to comply with the code of practice ("the Code") to be issued under the new section 98O, it is up to the Advisory Body to determine what details of complaints and findings will be disclosed to the public in the light of the governing law on data protection. For example, data protection principle 3 ("DPP3") under Schedule 1 to the Personal Data (Privacy) Ordinance (Cap 486) provides that "[p]ersonal data shall not, without the prescribed consent of the data subject, be used for a new purpose". A new purpose is defined to mean any purpose other than "(a) the purpose for which the data was to be used at the time of the collection of the data; or (b) a purpose directly related to the purpose referred to in paragraph (a)". "Data subject", in relation to personal data, is defined in section 2 of Cap. 486 to mean the individual who is the subject of the data. "Personal data" is defined in section 2 of Cap. 486 to mean any data –

(a) relating directly or indirectly to a living individual;
(b) from which it is practicable for the identity of the individual to be directly or indirectly ascertained; and
(c) in a form in which access to or processing of the data is practicable. (emphasis added)

18. It may be noted that third party funders typically adopt a variety of publicly listed and private corporate organisational structures (see para. 3.16 of the LRC Consultation Paper). If the complaints lodged against the third party funders not only cover corporate affairs but also involve an individual's misconduct, then the information may fall within the definition of "personal data" in Cap. 486 and the disclosure of the personal data to the public would constitute a new purpose in contravention of DPP3.

19. Subject to the above Cap. 486 considerations, details of any findings by a court of a third party funder's failure to comply with the Code should have already been recorded and made known to the public through the publication of the court judgment, subject to the requirements of section 17 of the Arbitration Ordinance (Cap 609). The findings by an arbitral tribunal of the failure of a third party funder to comply with the Code may not fall within the meaning of "any information relating to the arbitral proceedings under the arbitration agreement or an award made in those arbitral proceedings" under the prohibition against disclosure under section 18(1) of the Arbitration Ordinance (Cap. 609).

20. In view of the above, it appears that whether the details of complaints and findings made against the third party funder could be made known to the public would depend on the facts and circumstances of each case.

(e) Express Power of the Advisory Body to disclose

21. As noted by the LRC Sub-committee, there is little uniformity in the form of regulation of third party funding in jurisdictions where third party funding is permitted. The main trend is towards a "light touch" approach to regulation either by including statutory regulation of financial and conflict issues (e.g. Australia) or self-regulation (e.g. England and Wales). (Consultation Paper paragraphs 4.6, 4.8 and 6.6)

22. In Australia, there is only limited regulation of third party funding under the federal legislation governing the financial services industry. This legislation requires that third party funders have in place adequate procedures and practices for managing conflict of interest. (Consultation Paper paragraph 4.34)

23. In England and Wales, the litigation funding industry is self-regulated through the Association of Litigation Funders ("ALF"), although membership is not compulsory. The ALF system of regulation is set out in the ALF Code developed by the Civil Justice Council. 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. The ALF has complaint procedures in place, under which sanctions can be imposed. However, the main force of industry self-regulation is intended to come from the market credibility to be gained by third party funders who comply with the code. (Consultation Paper paragraphs 4.51-4.52, 4.81)

24. The LRC considers that the use of codes of conduct to promote best practices in the interests of the public is common in Hong Kong, including in the financial services sector. See, for example, the relevant codes adopted by the Securities & Futures Commission, the Hong Kong Federation of Insurers and the Hong Kong Monetary Authority. The LRC takes the view that a code is in line with the "light touch" approach to regulation adopted in other jurisdictions including Australia and England and Wales, while being a common way in Hong Kong of ensuring that high standards of probity, accountability and transparency are set. (LRC Report, paragraphs 5.20, 5.29)

25. We adopt the LRC's recommendation on taking a "light-touch" approach to regulation. Hence, we propose by way of the new section 98O in the Bill to empower an authorized body (to be appointed under the new section 98W(2)) to issue the Code setting out practices and standards for third party funders to follow when they carry on activities in connection with third party funding of arbitration. In line with the "light touch" approach, we propose, by way of the new section 98Q(6), to make clear that the Code is not subsidiary legislation. The proposed new section 98R(1) provides that a failure to comply with a provision of the Code does not, of itself, render any person liable to any judicial or other proceedings. The proposed new section 98R(2) provides, however, that the Code is admissible in evidence in proceedings before any court or arbitral tribunal, and that any compliance, or failure to comply, with a provision of the Code may be taken into account by any court or arbitral tribunal if it is relevant to a question being decided by the court or arbitral tribunal.

26. The LRC also recommends that a "light touch" approach to regulation, in the form of a code, should be adopted for an initial period of 3 years, and the code would not be subsidiary legislation. (LRC Report

paragraphs 5.20, 5.29) As a more long-term initiative, the LRC recommends that after the conclusion of the first three years of operation of the Code, the Advisory Body should issue a report reviewing its operation and make recommendations as to the updating of the ethical and financial standards set out in it. At this time the Advisory body should also make recommendations on whether a statutory or another form of body is needed, how it could be set up and the criteria for selecting members of such a body. In the meantime, the Advisory Body could at the end of each year review whether or not to speed up the process for regulation by an independent statutory or other form of body. The report should also deal with the effectiveness of the Code and make recommendations as to the way forward.

27. At the moment, although complaints can be referred to the Advisory Body, the Bill does not give express powers to the Advisory Body to examine and investigate any complaints received. This is of particular relevance if a third party funder will be named merely by reason of a complaint having been made against it. It is possible that the complaint is ultimately found not to be substantiated. As a matter of fairness, before the Advisory body decides to name a specific third party funder for its failure to comply with the Code, the third party funder in question should be given the right to make representation. If an adverse decision against it is made to disclose its identity to the public, the third party funder should be given channels of review or appeal against that adverse decision.

28. In the light of the above consideration, it is up to the Advisory Body to consider and decide what detailed information should be disclosed to the public when it monitors and reviews the operation of the new Part 10A as envisaged under the new section 98W(1).

29. If it is felt that the Advisory Body should be given express power to make public disclosure of the information, there will be a need to consider substantial amendments to the Bill for the introduction of the requisite statutory safeguards to ensure fairness to stakeholders. The Government considers that the likely amendments required would bring about a fundamental change to the nature of the Advisory Body. At this stage, the Government maintains its view that at the inception stage of the

third party funding industry in Hong Kong, a light touch approach should be adopted. The Government concludes that the introduction of a provision in the Bill to give an express power to the Advisory Body to disclose any information received pursuant to the new section 98P(1)(i) is not warranted at this stage. The Government agrees to adopt the LRC's recommendations that after the conclusion of the first three years of operation of the Code, the Advisory Body should issue a report reviewing its operation and make recommendations as to the updating of the ethical and financial standards set out in it (including whether it is necessary to introduce express power for the disclosure by the Advisory Body).

Yours sincerely,

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