Securing Funding; Securing Costs

Recent developments in litigation funding, DBAs, security for costs and non-party costs orders

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Damages Based Agreements

- Market remains constrained by DBA Regulations 2013 which are unclear in many respects.
- E.g. can lawyers be paid on conventional basis if DBA is terminated early by the client or if the client breaches the contract?
- Can you have hybrid DBA (i.e. lawyers get some fees come what may)?
- Can you be paid *before* costs are assessed when the CFA says lawyers cannot be paid more than the percentage net of any costs 'paid **or payable**' by the opponent? And who takes enforcement risk if solicitor has to give credit for costs merely 'payable' by the opponent?
- Innovation/boundary testing is inhibited by the sanction for getting it wrong: a non-fault based and non-discretionary statutory unenforceability.
- Various cases on the regulations appear to have settled, legislative reform has stalled.

Non-party costs orders ("NPCOs")

Costs jurisdiction provided by s.51 Senior Courts Act 1981:

"(1) Subject to the provisions of this or any other enactment and to the rules of court, the costs of and incidental to all proceedings…shall be in the discretion of the court…

(3) The court shall have full power to determine by whom and to what extent costs are to be paid."

Discretion conferred on the Court in wide terms. First established in *Aiden Shipping Co Ltd v Interbulk* (1986) that the discretion extended to third parties: i.e. the power to make an NPCO.

Procedural gateway – CPR r.46.2. No express or defined limitation on circumstances in which an NPCO may be made. The main thrust of the rule is the need for joinder. This is usually (not always) a formality.

Potential Targets

- Controllers & Promoters

- Commercially Interested Funders

- Lawyers

- Insurers

- Pure goodwill (disinterested funders)

Traditional Approach

- 'Exceptional' jurisdiction, where 'considerable caution' required (*Symphony Group v Hodgson* (1994)

- Orthodox approach to 'corporate veil': *Taylor v Pace Developments* (1991 – Lloyd LJ); *Mettaloy v MA UK* (1997 – Millett LJ)

'It is not, however, sufficient to render a director liable for costs that he was a director of the company and caused it to bring or defend proceedings which he funded and which ultimately failed. Where such proceedings are bought bona fide and for the benefit of the company, the company is the real plaintiff. If in such a case an order for costs could be made against a director in the absence of some impropriety or bad faith on his part, the doctrine of the separate liability of the company would be eroded and the principle that such orders should be exceptional would be nullified.' (Millett LJ)

The Sea Change: *Dymocks v Todd*

- Privy Council in *Dymocks Franchise Systems v Todd* (2005)

- 'Exceptional' just means 'outside the ordinary run of cases where parties pursue or defend claims for their own benefit and own expense'

- Ultimate question in any case is simply whether it is just to make the order

- 'Ordinarily' where non-party funds, controls or benefits from proceedings, so it is a 'real party' then it should pay the successful parties' costs

What Remains of the Corporate Veil?

- Lord Brown: liquidators and directors *may* be treated differently, if acting in interests of company, shareholders or creditors

- First domestic case: *Goodwood Recoveries v Breen* (2005, Rix LJ):

  '*the law has moved a considerable distance in refining the early approach in Taylor v Pace Developments. Where a non-party director can be described as the "real party", seeking his own benefit, controlling and/or funding the litigation, then even where he has acted in good faith or without any impropriety, justice may well demand that he be liable in costs*'

Threlfall v ECD Insight (2013)

Lewison LJ:

'*If a non-party costs order is made against a company director, it is quite wrong to characterise it as piercing the corporate veil; or to say that the company and the director are one and the same… the separate personality of a corporation, even a single-member corporation, is deeply embedded in our law. But its purpose is to deal with legal rights and obligations. By contrast, the exercise of discretion to make a non-party costs order leaves rights and obligations where they are. The very fact that the making of such an order is discretionary demonstrates that the question is not one of rights and obligations of a non-party, for no obligations exist unless and until the court exercises its discretion. Moreover the fact that the discretion, if exercised, is exercised against a non-party underlines the proposition that the non-party has no substantive liability in respect of the cause of action in question.*'

Sony/ATV v WPMC & Bailey (2018)

The director and majority shareholder of an unsuccessful defendant to a copyright claim appealed against an NPCO against him.

In allowing the appeal, the CA held *inter alia*:

(a) it is not necessary to identify a divergence of interest in order for an NPCO to be made against a company director;

(b) the so-called "Arkin Cap" should not be extended to cases where a company director is the "real party" to claim; but

(c) the absence of any warning of a potential NPCO application until over a year after judgment was handed down was fatal.

Shareholders & Directors: Predictability Post *Bailey*

Absence of 'bright lines' may cause difficulty, especially where companies and their controllers are essentially *alter egos*:

- 'In many cases it will be clear whether the case falls within the general rule or the exception, but in others the task of deciding on which side of the not very precise dividing line will be more challenging.'

- 'It may well not be just to impose an NPCO where a director is pursuing or defending proceedings in the interests of a group of shareholders all holding minority interests, but just to do so when it is in his interests alone.'

NPCOs against Solicitors

- Lawyers who fund litigation are not exposed to NPCOs in the same way as other commercial funders.
- A pure policy decision to encourage lawyers to fund litigation via CFAs, DBAs etc.
- Protection applies so long as lawyers do not do more than their usual function plus the funding.
- Usual rule: *Tolstoy v Aldington* (1996); *Flatman v Germany* (2013).
- Example of exception: *Myatt v NCB* (2007).

The "Arkin cap": *Arkin v Borchard Lines* (2005)

A claim against several defendants failed. Their costs were £6m. A commercial funder had provided funding of £1.3m for the claimant's expert reports and cost of organising documents.

If a professional funder, who is contemplating funding a discrete part of an impecunious claimant's expenses, is to be potentially liable for the entirety of the defendant's costs should the claim fail, no professional funder will be likely to be prepared to provide the necessary funding

A professional funder, who finances part of a claimant's costs of litigation, should be potentially be liable for the costs of the opposing party to the extent of the funding provided

Extra-judicial doubt cast on the "Arkin cap"

"**Review of Civil Litigation Costs: Final Report**" Dec 2009

Chapter 11 – concerning third party litigation funding and costs liability:

- At paragraphs 4.3 and 4.4, Sir Rupert set out criticisms of the "Arkin cap" which he had received during the consultation phase of preparing the Jackson Report.
- At paragraph 4.5, he confirmed that: *"…the criticisms of Arkin are sound. There is no evidence that full liability for adverse costs would stifle third party funding or inhibit access to justice."*
- At paragraph 4.6, he stated: *"In my view, it is wrong in principle that a litigation funder, which stands to recover a share of damages in the event of success, should be able to escape part of the liability for costs in the event of defeat. This is unjust not only to the opposing party (who may be left with unrecovered costs) but also to the client (who may be exposed to costs liabilities which it cannot meet."*

Development of funder liability

Excalibur Ventures v Texas Keystone (2017)
£17.5m advanced by funders for security. Claim dismissed and indemnity costs ordered against C. Funders joined for the purposes of costs. No issue as to ability to cover D's costs – primarily a dispute on apportionment between funders.

Three points of principle:

(1) Funders should be liable on the indemnity basis
- No principled basis for funder to dissociate itself from conduct of those he had enabled to litigate and on whom he relied to make a return.
- The funder took a risk which he could investigate before offering funding and during the course of the litigation.
- Ongoing review of the progress of litigation by lawyers independent of those conducting the litigation was essential to reduce the risk of indemnity costs.

(2) It was not disputed that the "Arkin cap" applied, but it was noted that ""*some consider the [Arkin cap] to be over-generous to commercial funders"*

(3) Sums provided by way of security for costs should count towards the "Arkin cap" thereby increasing the liability of the funders.

Further (judicial) doubt cast on the "Arkin cap"

Bailey v GlaxoSmithKline UK Ltd (2018)

Application for security for costs against Cs' funder, Managed Legal Solutions Limited. MLS relied on an ATE insurance policy and on its own liability as a funder being subject to the "Arkin cap".

Foskett J:

(a) here the funder could not rely on the "Arkin cap" at the security for costs stage: the decision in *Arkin* had been criticised, and a challenge to it might be made, particularly where the funder underwrote the whole of C's costs or where the funding arrangements were objectionable in some way;

(b) though the ATE policy did not contain an anti-avoidance provision, the court could, at the security for costs stage, attribute some value to the ATE policy. As the policy provided£750,000 cover, and assessing the risk of avoidance at 1/3, the amount of security ordered was reduced by £500,000.

Arkin considered: *Re Angel House Developments Ltd*

Two claims heard together, brought by Ms Davey: against lender and former administrators. Comprehensive dismissal and indemnity costs ordered against her. No payment made. Combined costs total £7m+. If "Arkin cap" were imposed, the funder's liability would be limited to c.£1.3m.

Application of the "Arkin cap" under sustained assault. Points made include:

- Application in this instance would be unjust;
- The "Arkin cap" has never been applied to deprive a defendant of its costs recovery;
- The funding was unlimited in scope;
- Ms Davey's potential benefit from the litigation was illusory;
- The funding agreement was revised to (a) remove ATE, (b) reduce amount of funding, yet (c) retain same profit for the funder;
- Advice of excellent prospects of success such that limitation of exposure would render reward disproportionate.

Against that, the funder contends that the "Arkin cap" should apply,

Judgment awaited…

Non-party costs orders against insurers

Travelers v XYZ (2018)

1000 claimants joined a GLO relating to defective breast implants.

623 claims were against Transform Medical Group.

Of those, 197 insured by Travelers, 426 uninsured.

Insured claims were settled; Travelers paid their damages and share of costs.

Transform went into liquidation.

Uninsured claimants successfully sought costs against Travelers under s51.

Travelers cont.

Travelers argued that an insurer would only be liable if it controlled litigation in its own interest, ignoring inconsistent interests of its insured.

CA upheld the order:

- the cases do not lay down conditions to be satisfied before costs may be ordered against insurers;
- an order will be exceptional, but judged against the whole range of litigation;
- reciprocity is important: if the claim had failed, Travelers would benefit from Transform's costs being paid by insured and uninsured claimants; if the claim succeeded it should equally be liable for all their costs.

Permission to appeal granted by Supreme Court

Various Claimants v Giambrone (2019)

Cs' claim succeeded at trial for equitable compensation from the Defendant law firm, which acted on their purchases of property in Italy.

The Claimants applied for costs against Giambrone's insurers, AIG, under s51.

AIG denied it controlled the litigation, having ceded conduct to Giambrone.

Foskett J ordered costs against AIG:

> "*where an indemnity insurer substantially relinquishes control of the conduct grounds for intervening), and does so in the expectation that it will be immune from a costs liability towards the opposing party if the opposing party is successful, that expectation is open to be falsified by the court in a section 51 application, particularly if the prospects of success for the insured are assessed as poor.*"

Security for costs

CPR 25.14

An order may be made against a person who:

"*has contributed or agreed to contribute to the claimant's costs in return for a share of any money or property which the claimant may recover in the proceedings.*"

Security against funders: relevant factors

RBS Rights Issue Litigation (2017 Hildyard J)

Has the non-party become in all but name a real party

Is there a real risk of non-payment such that security should be granted

Is there a sufficient link between the funding and the costs sought

Has a risk of costs been sufficiently brought home to the non-party

Are there factors, including delay, to tip the overall balance against an order

In the matter of Hellas Telecoms (2017)

1. there is a power inherent/implied in CPR 25.14 to make orders so as to enable an effective application to be made
2. even where there was no pre-existing costs order against anyone in the proceedings
3. Snowden J ordered Cs to disclose identity of the funders and details of funding arrangements.

ATE as security

Premier Motor-auctions v PWC (2016)

- D was "entitl*ed to some assurance that [the insurance] was not liable to be avoided for misrepresentation or non-disclosure"*
- The policy did not provide sufficient protection : court could not evaluate the risk of avoidance

Recovery Partners v Revoker (2018)

- Taken together, a deed of indemnity as well as an ATE policy provided adequate security

St Vincent v Robinson (2018)

- An ATE policy, together with endorsements and a letter of clarification, was a sufficient answer to the application for security
- The endorsements ensured that the policy was non-voidable

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