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THIRD PARTY FUNDING OR LITIGATION FUNDING

SIXTH LECTURE IN THE CIVIL LITIGATION COSTS REVIEW IMPLEMENTATION PROGRAMME

THE ROYAL COURTS OF JUSTICE

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"The human species, according to the best theory I can form of it, is composed of two distinct races, the men who borrow, and the men who lend."[1]

1. INTRODUCTION

1.1 I am delighted to attend this gathering of litigation funders and others, to mark the launch of the new Code of Conduct. Under Lamb's classification, litigation funders would very roughly fall into the second category of humanity.[2] In order not to disrupt such a jovial occasion, I shall hand down this lecture in writing for those who wish to read it over their glass of wine, and confine my oral presentation to a brief synopsis of the lecture.

1.2 This lecture. This is the sixth lecture in the present series. The previous five lectures can all be accessed on the Judiciary website.[3] This lecture, like the previous ones, has paragraph numbers for ease of cross-reference.

1.3 Terminology. The title of this lecture is somewhat longwinded, because the nomenclature has recently changed. What used to be called "third party funding" is now more commonly called "litigation funding". I shall use the latter term in this lecture, although "third party funding" was the term used in my two reports. I shall refer to the Civil Litigation Costs Review as "the Costs Review". I shall refer to the Costs Review Preliminary Report as "the Preliminary Report" and the Costs Review Final Report as "the Final Report". I shall use the abbreviation "CFA" for conditional fee agreement.

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[1] Charles Lamb, *The Two Races of Men,* Essays of Elia, 1823

[2] Hopefully the clients are an improvement on Lamb's first category: "What a careless, even deportment hath your borrower! What rosy gills! What a beautiful reliance on Providence doth he manifest, taking no more thought than lilies! What contempt for money …"

[3] www.judiciary.gov.uk

2. BACKGROUND

2.1 A late arrival. The funding of claims by commercial bodies in return for a share of the proceeds has been a late arrival on the litigation scene. This is because outside interference of this nature was long regarded as morally reprehensible (since it stirred up litigation) and unlawful (because of the doctrines of maintenance and champerty).

2.2 Narrowing of maintenance and champerty. Maintenance and champerty remain as torts.[4] However, their scope has been progressively narrowed by judicial decisions: see, for example, the recent decision of the Court of Appeal in *Sibthorpe v Southwark Borough Council* [2011] EWCA Civ 25, [2011] 1 WLR 2111.

2.3 Properly structured litigation funding approved. It is now established that properly structured litigation funding does not infringe the rules against maintenance and champerty: see *Arkin v Borchard Lines* [2005] EWCA Civ 655, [2005] 1 WLR 3055. In describing a funding agreement which does not infringe, the court said this at [40]:

"Our approach is designed to cater for the commercial funder who is financing part of the costs of the litigation in a manner which facilitates access to justice and which is not otherwise objectionable. Such funding will leave the claimant as the party primarily interested in the result of the litigation and the party in control of the conduct of the litigation."

2.4 Developments between 2005 and 2009. The Court of Appeal's decision in *Arkin* brought litigation funding into the main stream in England. The High Court's majority decision in *Campbell's Cash & Carry Pty Ltd v Fostif Pty Ltd* [2006] HCA 41 had a similar effect in Australia.[5] The Civil Justice Council ("CJC") took up the baton. In 2005 the CJC published its report " Improved Access to Justice – Funding Options and Proportionate Costs " (authors M Napier, Judge P Hurst, R Musgrove, Prof Peysner). This proposed that "building on the judgment of the Court of Appeal in *Arkin* further consideration should be given to the use of third party funding as a last resort means of providing access to justice ". After debating these matters in a forum the CJC published a further report in 2007 entitled " Improved Access to Justice – Funding Options and Proportionate Costs " (authors M.Napier, Judge P Hurst, Prof Moorhead, R Musgrove, C Stutt). Recommendation 3 of that Report said:

> "Properly regulated Third Party Funding should be recognised as an acceptable option for mainstream litigation.Rules of Court should also be developed to ensure effective controls over the conduct of litigation where third parties provide the funding."

Following further forum discussions the CJC prepared a first draft voluntary code of conduct for "Third Party Litigation Funding". This draft code did not enter the public domain for a year. So its provisions could not be discussed in my Preliminary Report, although they could be and were discussed in the Final Report

2.5 Costs Review. The question of third party funding (as it was then still called) was one of the discrete issues considered during the Costs Review: see chapter 15 of the Preliminary Report and chapter 11 of the Final Report. My three recommendations in respect of third party funding were as follows:[6]

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[4] But not as crimes: see s. 14 (1) of the Criminal Law Act 1967

[5] For a discussion of the extensive use of litigation funding in Australia, see Preliminary Report, chapter 58 (Australia) para 4.6. At the time of my visit to IMF in Sydney, that company had supported approximately 200 cases, paying out adverse costs in those few cases which its clients had lost.

[6] Using the numbering in the list of recommendations at the end of the report, pages 463-467

"11. A satisfactory voluntary code, to which all litigation funders subscribe, should be drawn up. This code should contain effective capital adequacy requirements and should place appropriate restrictions upon funders' ability to withdraw support for ongoing litigation.

12. The question whether there should be statutory regulation of third party funders by the FSA ought to be re-visited if and when the third party funding market expands.

13. Third party funders should potentially be liable for the full amount of adverse costs, subject to the discretion of the judge."

2.6 Developments in 2010. These issues were considered at a number of events during 2010, including a litigation funding conference at Oxford University and a CJC stakeholder forum. At that forum a nascent Litigation Funders Association was formed and the CJC agreed to oversee the development of a suitable code of conduct for litigation funding. Between July and December the CJC conducted a consultation exercise on a draft code and draft articles for the Litigation Funders Association.

2.7 Preparation of the Code of Conduct in its final form. In early 2011 Michael Napier QC was appointed chairman of a CJC working party which was to develop the Code of Conduct in consultation with all interested parties. I pay tribute to Mike for the excellent and painstaking work which he has done in bringing this project to fruition. The finished product which you all have before you today has gone through innumerable drafts and it meets, so far as any draftsman reasonably can, the concerns which have been raised by the various stakeholder groups. The working party was kind enough to consult me from time to time and to invite me to speak at their seminar in May 2011.

2.8 The final product delivered by the working group comprises:
Code of Conduct for Litigation Funders ("the Code")
Rules of the Association for The Association of Litigation Funders of England & Wales ("the Rules").

2.9 Link between the Code and the Rules. Rule 6.1 of the Rules requires every member of the The Association of Litigation Funders of England & Wales to abide by the Code, to the extent that it applies to them.

3. THE CODE OF CONDUCT IN ITS FINAL FORM

3.1 A clear and straightforward document. Both the Code and the Rules are clear and straightforward documents, which belie the huge amount of effort and negotiation that have gone into their drafting. The Rules require all members of the Association to abide by the Code. The Code sets out the obligations of funders in a short and clear document. The litigation funding agreement between funder and client is referred to as "LFA". I attach the final version of the Code as an appendix.

3.2 My original concerns. My particular concerns originally were as follows:

(i) That there should be proper provision for capital adequacy. (The provision in the original draft code that the funder should be able to meet its liabilities for the next three months was plainly inadequate.)

(ii) That the funder should not be entitled to terminate the funding agreement mid-litigation

without good reason. (The original draft code appeared to permit this.)

(iii) That the extent of the funder's ability to influence the litigation and any settlement negotiations should (a) be properly restricted and (b) defined with clarity.
See chapter 11 of the Final Report.

3.3 Those concerns have been met. Nothing is certain in this sublunary world and no contract is totally watertight. However, in my view the final version of the Code meets each of those concerns to a reasonable extent.

Capital adequacy

3.4 Clause 7. Capital adequacy is addressed in clause 7 of the Code, which provides:

"A funder will:

"(d) maintain at all times adequate financial resources to meet its obligations to fund all of the disputes that it has agreed to fund, and in particular will maintain the capacity:
(i) to pay all debts when they become due and payable; and
(ii) to cover aggregate funding liabilities under all of its LFAs for a minimum period of 36 months."

3.5 Comment. This is a very substantial improvement upon the original provision.[7] Obviously there are cases which will run for more than three years, although such cases are becoming rarer and I hope that other pending reforms will further reduce their number. Nevertheless, as a provision in a code to which funders are expected to sign up voluntarily, in my view this clause strikes a reasonable balance between practicality and client protection.

Withdrawal

3.6 Clauses 9 and 10. Clauses 9 and 10 of the Code provide:

"9. The LFA shall state whether (and if so how) the Funder may:
...
(b) terminate the LFA in the event that the Funder:
(i) reasonably ceases to be satisfied about the merits of the dispute;
(ii) reasonably believes that the dispute is no longer commercially viable; or
(iii) reasonably believes that there has been a material breach of the LFA by the Litigant.

10. The LFA shall not establish a discretionary right for a Funder to terminate a LFA in the absence of the circumstances described in clause 9(b)."

3.7 Comment. Again these provisions are a very substantial improvement upon the original draft[8] and they achieve a fair balance between the interests of funder and client. There is also to be a QC clause in every LFA to deal with disputes between funder and client.

[7] See Final Report, chapter 11, para 2.9.
[8] See Final Report, chapter 11, para 2.7.

Control

3.8 Clause 7. Clause 7 of the Code provides:

"7. A Funder will:

(a) take reasonable steps to ensure that the Litigant shall have received independent advice on the terms of the LFA, which obligation shall be satisfied if the Litigant confirms in writing to the Funder that the Litigant has taken advice from the solicitor or barrister instructed in the dispute;

(b) not take any steps that cause or are likely to cause the Litigant's solicitor or barrister to act in breach of their professional duties;

(c) not seek to influence the Litigant's solicitor or barrister to cede control or conduct of the dispute to the Funder; …"

3.9 Comment. This provision should prevent the Funder from usurping control of the litigation in a manner which would infringe the principles referred to in *Arkin*. On the other hand the funder has a stake in the litigation. It is or should be entitled to be consulted. In addition funders build up substantial experience in the fields of litigation in which they operate. Therefore their views may on occasions be a positive asset for the client and its legal team.

4. GENERAL

4.1 Importance of the Code. The publication of the Code is an important event. I anticipate that solicitors will be advising their clients only to enter funding agreements with litigation funders who sign up to the Code and comply with its provisions.

4.2 The new landscape. There will be a new litigation landscape after 2012, if Part 2 of the Legal Aid, Sentencing and Punishment of Offenders Bill is enacted in its present form. There is likely to be a greater role for litigation funders, if CFA success fees cease to be recoverable. This suggestion is borne out by the experience of Australia, where success fees have never been recoverable: see chapter 58 of the Preliminary Report at paras 2.7, 2.8, 4.2 and 4.6. For an up to date review of litigation funding in Australia, see Michael Legg's recent article in Civil Justice Quarterly.[9]

4.3 A wider range of claims? I express the hope that in the future litigation funders will be able to support a wider range of litigation than at present, including group actions and claims of lower value.

4.4 The range of funding options. The use of commercial litigation funders is just one means of financing litigation. Other means which will become available when (and if) the Final Report is implemented are contingency fees,[10] a Supplementary Legal Aid Scheme[11] and hopefully a Contingent Legal Aid Fund,[12] as well of course as CFAs without recoverable success

[9] *Reconciling Litigation Funding and the Opt Out Group Definition in Federal Court of Australia Class Actions* (2011) CJQ 52, in particular section 2.2

[10] See clause 42 of the Bill. Contingency fees will be the subject of a later lecture in this series.

[11] To which the government is now committed: see the MoJ's response to the legal aid consultation published on 21st June 2011.

[12] The Bar Council's CLAF Group is now actively pursuing this option. See the second lecture in this series: http://www.judiciary.gov.uk/media/speeches/2011/lj-jackson-speech-contingency-legal-aid-fund.

fees.

4.5 Conclusion. Today's publication of the Code will mark the satisfactory implementation of recommendation 11 in the Final Report, provided that all reputable litigation funders are willing to join the Association of Litigation Funders and sign up to the Code. My understanding is that they are so willing. The Association will promote the public interest by enabling properly viable claims to be pursued, including no doubt some claims which ultimately are unsuccessful. I wish the Association well.

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APPENDIX

CIVIL JUSTICE COUNCIL
STRICTLY PRIVATE & CONFIDENTIAL
CODE OF CONDUCT for LITIGATION FUNDERS

1. This code (the Code) sets out standards of practice and behaviour to be observed by Funders who are Members of The Association of Litigation Funders of England & Wales (The Association).

2. A Funder has access to funds immediately within its control or acts as the exclusive investment advisor to an investment fund which has access to funds immediately within its control, such funds being invested pursuant to a Litigation Funding Agreement (LFA) to enable a Litigant to meet the costs of resolving disputes by litigation or arbitration (including pre-action costs) in return for the Funder:

   (a) receiving a share of the proceeds if the claim is successful (as defined in the LFA); and

   (b) not seeking any payment from the Litigant in excess of the amount of the proceeds of the dispute that is being funded, unless the Litigant is in material breach of the provisions of the LFA.

3. A Funder shall be deemed to have adopted the Code in respect of funding the resolution of disputes within England and Wales.

4. The promotional literature of a Funder must be clear and not misleading.

5. A Funder will observe the confidentiality of all information and documentation relating to the dispute to the extent that the law permits, and subject to the terms of any Confidentiality or Non-Disclosure Agreement agreed between the Funder and the Litigant.

6. A Litigation Funding Agreement is a contractually binding agreement entered into between a Funder and a Litigant relating to the resolution of disputes within England and Wales.

7. A Funder will:

   (a) take reasonable steps to ensure that the Litigant shall have received independent advice on the terms of the LFA, which obligation shall be satisfied if the Litigant confirms in writing to the Funder that the Litigant has taken advice from the solicitor or barrister instructed in the dispute;

   (b) not take any steps that cause or are likely to cause the Litigant's solicitor or barrister to act in breach of their professional duties;

   (c) not seek to influence the Litigant's solicitor or barrister to cede control or conduct of the dispute to the Funder;

   (d) maintain at all times adequate financial resources to meet its obligations to fund all of the disputes that it has agreed to fund, and in particular will maintain the capacity:

      (i). to pay all debts when they become due and payable; and to cover aggregate funding liabilities under all of its LFAs for a minimum period of 36 months. to cover aggregate funding liabilities under all of its LFAs for a minimum period of 36 months.

      (ii). to cover aggregate funding liabilities under all of its LFAs for a minimum period of 36 months.

8. The LFA shall state whether (and if so to what extent) the Funder is liable to the Litigant to:

   (a) meet any liability for adverse costs;

(b) pay any premium (including insurance premium tax) to obtain costs insurance;

(c) provide security for costs;

(d) meet any other financial liability.

9. The LFA shall state whether (and if so how) the Funder may:

(a) provide input to the Litigant's decisions in relation to settlements;

(b) terminate the LFA in the event that the Funder:

(i). reasonably ceases to be satisfied about the merits of the dispute;

(ii). reasonably believes that the dispute is no longer commercially viable; or

(iii). reasonably believes that there has been a material breach of the LFA by the Litigant.

10. The LFA shall not establish a discretionary right for a Funder to terminate a LFA in the absence of the circumstances described in clause 9(b).

11. If the LFA does give the Funder any of the rights described in clause 9, the LFA shall provide that:

(a) if the Funder terminates the LFA, the Funder shall remain liable for all funding obligations accrued to the date of termination unless the termination is due to a material breach under clause 9(b)(iii);

(b) if there is a dispute between the Funder and the Litigant about settlement or about termination of the LFA, a binding opinion shall be obtained from a

Queen's Counsel who shall be instructed jointly or nominated by the Chairman of the Bar Council.