The Law Society Gazette

Roundtable: litigation funding

13 March 2017

Litigation funding is increasingly lauded as a model for modern litigation. But its role in boosting 'access to justice' is less clear cut, the *Gazette*'s latest roundtable heard.

Last year, litigation funders committed some £723m to legal claims, according to research by City firm Reynolds Porter Chamberlain. That is a 25% increase on the previous year, and is evidence – if any were needed – that business is booming in the funding industry.

At the *Gazette*'s latest roundtable, lawyers discussed the impact funding is having on litigation and where it is heading.

Last month the *Gazette* reported that Australian funder IMF Bentham had launched a new $200m vehicle to fund US cases; while in the UK, funder Calunius raised £100m in November. It seems that every few months, there is another big announcement of more cash being pumped into the sector. So why do funders seem to be knocking on an open door when it comes to raising capital?

As Rachel Rothwell, editor of *Gazette* sister publication *Litigation Funding*, explains, funding is an attractive asset class because it is distinct from the highs and lows of the economy – and can offer excellent returns if funders pick the right cases. In the UK, litigation funding is endorsed by the senior

judiciary – the most recent example being the opening line of November's *Excalibur* judgment, which states matter-of-factly that 'third-party funding is a feature of modern litigation'.

She adds: 'The more the industry grows, the more mainstream it becomes – which encourages investors further and fuels even more growth.'

Robert Dougans, commercial litigator at Bryan Cave, highlights another reason why investors are putting their cash into litigation: 'Money is seeking new returns because interest rates are effectively negative… You are going to see people chasing speculative returns, because whereas you used to be able to put pension funds and institutional money in gilts and FTSE 100 stocks and get something of a return on your investment, now you just can't. People have to seek other returns.'

Raising capital is just one side of the coin for funders; they also need to find cases to invest in. Here, too, we are seeing a shift. The panel reports that funding has moved beyond its starting point as a lifeline for impecunious claimants, to become an attractive option for bigger and better-financed corporates.

Maurice Power is managing director of litigation funder Ferguson Litigation Funding, a relatively new market entrant, which sponsored this roundtable. He observes that one of the factors driving clients towards funding is the 'tension' between general counsel and financial directors – with the latter keen to keep litigation risk off the balancesheet. 'Companies are looking for outside funding to pursue meritorious claims, but also to quieten the financial director's fears about the impact it will have on the profitability of the business,' he says.

Clive Zietman, head of commercial litigation at Stewarts Law, which acted for institutional investors in a high-profile shareholder action against RBS which settled in December, detects a 'marked trend' relating to attitudes towards funding in recent years. He says: 'I think there was a time when funding was [primarily for] the impoverished claimant for the reasonably sized claim, whereas now there's much more institutional interest.' Zietman observes that institutions have come to recognise funding as 'a sensible way of managing risk'. They are happy to give away some equity in the success of the case, in exchange for certainty over exposure.

David Greene, senior partner at Edwin Coe with more than 30 years' experience of class actions – his first being a legal action stemming from the 1988 Lockerbie bombing – has a long history of working with funders.

He has also seen a shift in attitudes among financial institutions, particularly relating to shareholder claims.

He says: 'The City was really quite conservative about [shareholder actions] – they didn't like suing their mates down at the City club. That has changed, and I think, actually, the RBS case has changed that culture quite substantially. The institutions are now seeing funding as a possibility, in giving them flexibility in a case, and some offloading of cases.'

As a class action lawyer, Greene finds that the funding available for this type of claim has become far more flexible than it used to be. One key change is that funders will now assist in book-building the claim, something that would never previously have happened and is very useful in building the case.

'I think with competition and maturity, the market has changed quite a bit for our purposes,' Greene remarks. 'We find it much easier now to start giving ideas to funders and say, "are you interested in this?" and they either say yes or no. Whereas previously they wanted some pretty cast-iron guarantees, they have now become more flexible. Funders have learned over time, they've had some winners and some losers – indeed some quite well-known losers – and this has given them the experience and maturity of assessing cases and being much more flexible.'

Access to justice

Litigation funding is often held up as a means of helping litigants to secure 'access to justice', but the panel was sceptical.

For Frances Coulson, head of litigation and insolvency at Moon Beever, funding does little to help ordinary people. 'It's sold as access to justice – it's not access to justice,' she asserts. 'If you are acting for Mrs Bloggs who wants to sue her builder for £30,000, you have no chance of funding. The true problem there is the state of the courts. A lawyer simply can't run a cost-efficient case in that sort of arena – you might have to write to the court 30 times to get anything out of them, for example'.

Coulson's reservations are echoed by Grainne Barton, a clinical negligence solicitor at Hugh James in London. She is particularly concerned by the prospect of fixed costs, warning that 'fixed fees cannot work for us with the court system as it stands. You are not going to get paid for chasing 30 calls'.

Barton is also worried about the impact of the £10,000 court fee on claimants. Could litigation funding provide any answers? Barton has 'started to see some approaches' from funders in the clinical negligence arena, and adds that some solution is certainly needed to '[level] the playing field' with defendants.

Masood Ahmed, member of the Civil Procedure Rule Committee and a lecturer at the University of Leicester, recalls the way third-party funding was viewed by Lord Justice Jackson in the context of his costs reforms.

He says: 'When Jackson came out with his report, he praised the funding of litigation. He was keen on this as one way in which access to justice can be increased. But clearly, from this discussion, it is not necessarily working for individuals.

'Yes, third-party funding seems to be working for big corporates, banks and so forth, and those with deep pockets who can take the risk. But for Joe Bloggs, it's going to be extremely difficult. There's a real issue there about how we can come up with effective models to try to widen access to justice through funding.'

On the subject of Jackson, Marvin Simons, who heads the litigation practice at Seddons, is worried about the impact that the Legal Aid, Sentencing and Punishment of Offenders Act is having on the balance of power in litigation.

He says: 'I think it has tipped the balance of litigation away from the claimant to the defendant in many cases. We act for both, although we're probably more claimant than defendant, but in the old days, the worst thing you got as a defendant was notice of funding. That was terrible news; but as claimants you don't serve those any more – though you almost feel as though you want to serve one anyway.

'So that's gone and now, instead of the pressure being on the defendant, the pressure is actually coming back on to the claimant.'

Judge's red line

Simons describes a recent case in which his client had a very strong claim, with damages up to £300,000. But in the county court, the district judge drew a red line through so much of the budget (including the use of a forensic accountant) that it severely affected the dynamic of the case, weakening the claimant's position.

'In the longer term, this is going to mean that a lot of defendants – if they're getting savvy to this – will think, "let's sit tight and do nothing, and just wait for them to run out of money". The defendant will think, maybe they will decide that it's not worth paying the funders three-quarters of the value of the

claim if they go all the way to trial, because it only stacks up if they settle this early. So let's sit tight". Then, I think defendants will actually do better from this than claimants.'

Nick Pontt, head of financial services litigation at Browne Jacobson, adds: 'There is another factor that is going to become a huge play for large companies – the funding of defence work. So, a company may have deep pockets, but it doesn't need to reach into them because it can agree terms that as long as the claim doesn't reach a cap in success, whether that's a settlement or determination, then the funder makes money. That may further slide towards the defendants.'

Returning to Ahmed's question regarding the type of models that could be used to plug the justice gap, views are mixed on the extent to which funding can be made to work for lower-value commercial litigation. One relatively recent trend that may hold the answer is for funders to provide finance not for individual cases, but for a group – or 'portfolio' – of claims which may be of lower value individually.

At the table

Eduardo Reyes, *Law Society Gazette*; Andy Ellis, Practico; Robert Dougans, Bryan Cave; Marvin Simons, Seddons; Masood Ahmed, Civil Procedure Rule Committee; PJ Kirby QC, Hardwicke chambers; Grainne Barton, Hugh James; David Greene, Edwin Coe; Clive Zietman, Stewarts Law; Michael Frisby, Stevens & Bolton; Nick Pontt, Browne Jacobson; Frances Coulson, Moon Beever; Maurice Power, Ferguson Litigation Funding; Rachel Rothwell, *Litigation Funding* magazine; Matthew Kain, Kain Knight

Pontt says: 'I'm interested in the new entrants to the litigation funding market who will look at portfolios of smaller claims, who will fund deals that require investigation at the front.

'The question is, what deal can you reach with the funder? What are the metrics that empower or disempower the claimant to bring or defend the claim? As new entrants join the market, and competition increases, my hope is that those metrics will justify smaller investment and empower some claimants, and give corporates a way to off-book litigation. I can see the merits in that from a risk-profile perspective.'

Power explains Ferguson's approach regarding the size of the claims it will fund. He says: 'We're interested in any size of claim; for example we've recently got one that is settling at £40,000 on an insolvency. [In insolvency] there are also funders out there that are looking to monetise claims, to actually purchase claims for a cost.

'So the smaller claim is still actionable and workable, but it still has to make commercial sense. And it still has to be in the claimant's favour – the claimant has to come out of this with something.'

Power adds that Ferguson has been approached by law firms to offer a joint venture portfolio product, that would be jointly funded by Ferguson and the law firm. 'The risk for us, as a funder looking at portfolio ranges, is that you get negative selection for the cases that the solicitors don't want to run,' he says. In other words, the danger for funders is that law firms would run the best cases themselves under a conditional fee agreement or damages-based agreement, and only use funding on the riskier litigation.

'There's a balancing act, and we're still going through this evolution,' says Power. 'Funders will take a critical view and a commercial view of what is the right package and the right product, and the right risk to take.'

Proactive and dynamic

Power adds that the funder's relationship with a law firm is very important when considering portfolio arrangements: 'You need to understand how the firm works, and timeframe is important for us. As a funder, the longer our money is out there the more at risk it is. So a law firm needs to be proactive and very dynamic for it to make sense for us.'

Simons highlights the difference LASPO has made in relation to small to medium-sized claims, and whether or not to involve funders. He says: 'Pre-LASPO, usually if you had a case for £1m, or even half a million or indeed £2m, if it was a really strong case then your best advice to the client would be to use a CFA. That way the client would get all their money back and you would get the success fee back. So it was rare that you would have a case where you could even justify thinking about [using funding].

'But that has completely turned on its head now. You end up saying to clients, "you don't actually want a CFA, because that means you're going to pay me more. If you win the case, you've still got to pay me another 100% or 50% [of costs], whatever it is, and how does that help you?" So the client isn't any better off…

'Funding then becomes a much more attractive option and some of the funders are now looking at the market for smaller claims. For example we have what they call "early funding" for a client with a shareholder dispute that is worth about £2m. So it's not a very big claim in those terms, but it's a situation where the client doesn't want to spend money, [and] he's prepared to pay the funder a fair amount to get the clout behind him so he can proceed with the claim.'

Simons suggests that for claims of this size, funding is 'expanding it to a whole area of litigation that just wasn't feasible before'.

Essar ruling

In the context of international arbitration, a judgment last October (*Essar Oilfield Services Ltd v Norscot Rig Management Pvt Ltd* [2016] EWHC 2361 (Comm)) could potentially be a game-changer for funding. HHJ Waksman upheld an arbitrator's decision to allow a successful claimant in an ICC arbitration to recover not only their legal costs, but also the cost of funding, which amounted to nearly £2m. The arbitrator had been very critical of the defendant's conduct in the litigation, which he said had been an 'attempt to cripple' the claimant financially.

Michael Frisby, a partner at Stevens & Bolton, notes that 'funders have got their sights set on international arbitration'. He says *Essar* is 'causing some consternation in the arbitration world, because you've effectively got strangers to the arbitration process getting involved, and the other party not necessarily knowing that they're even there, or are involved. This is causing difficulties for the [arbitration] institutions, [which do not know] quite how to deal with it.'

Frisby notes that considerable differences are emerging in relation to costs recovery in arbitration as opposed to litigation.

Andy Ellis, director of costs firm Practico, agrees. He says: 'One thing that has stuck in my mind over the last few months is what a different approach there might be from litigation to arbitration.

'In *Essar*, [the claimant recovered] everything with the cream on top; the funder's premium and everything else. And yet you look at civil litigation, and we could spend an hour and a half with our heads in our hands about which way cost recovery is going there. So the state of the divergence is enormous, potentially. But of course it's worth remembering that the recovery in *Essar* was in very fact-specific circumstances.'

Regulation

The funding industry is currently regulated not by government but instead a body called the Association of Litigation Funders. This was set up by a group of funders in 2011 for self-regulation of the industry, with the approval of Lord Justice Jackson. Funders who want to join must ensure they maintain access to at least £5m of capital and agree to abide by the association's code of conduct.

The government confirmed in January that it has no plans to move away from the system of voluntary regulation. But is it likely to stay that way?

Rothwell suggests that, as long as funding is primarily used for corporate clients, regulation of the industry is 'not really a priority for the government'. But she adds that this may change if funding becomes more prevalent in other fields (such as clinical negligence) for individual rather than corporate clients.

Power observes: 'My view on the self-regulation of litigation funding is that this is almost done on a case-by-case basis, because of the relationships and the contracts we have with the claimants and the solicitors. If the funder is exerting or over-exerting pressure, or inputting into the action and giving direction, then obviously that's wrong and it needs to be addressed by the law firm that's running the case. So, I would suggest that the regulation is going to come out naturally, through the evolution of the contracts and the trading terms between the claimant, the solicitor and the funder.'

For Pontt, government regulation of the sector could be problematic: 'I find it difficult conceptually, because we're talking about product where we are not [always] sure what it really is – is it a private equity fund, is it a hedge fund? How is it run? Each vehicle is different under different mandates, and currently the hedge fund industry and the private equity fund industry – other than general financial regulations – are unregulated. So parliament would have to [address] questions about the wider hedge fund industry, which is probably the most powerful industry there is.'

PJ Kirby QC, a barrister at Hardwicke chambers, who represented the ALF in its recent submissions in the Excalibur case, sees value in the 'badge' of membership as providing important comfort to solicitors. Rothwell adds: 'You can't be in the ALF unless you've genuinely got the money… It's a difficult market and if you're not familiar with the players in that market, then ALF membership is an obvious sign of assurance that you are dealing with a respectable funder.'

Future of funding

Where do the panel believe that the funding industry is headed? For Kirby, the *Excalibur* ruling – in which the Court of Appeal highlighted the fact that funders have a part to play in the administration of justice – could signal a subtle change in the funding 'dynamic'. He says the court has given something of a 'green light' to funders to get more involved in discussions relating to the case, and to keep the litigation and the relevant evidence under constant review.

Power says: 'We're excited about the future and we believe litigation funding is here to stay. I think the [high-value litigation] end is well-occupied at the moment and there won't be any new entrants at that level. But there will be more funders coming into the medium- to small-sized market, offering innovative products, different ways of funding, and different remuneration packages that make them attractive for the smaller clients. It's an interesting and fluid market at the moment.'

Matthew Kain, managing director of costs firm Kain Knight, concludes the roundtable discussion. He believes funding will remain available for 'heavy commercial litigation', but ends with a note of caution: 'The challenges in funding the lower levels will be the proportionality test, and whatever Jackson does in relation to fixed recoverable costs. I think that could be a serious challenge for funders.'

- This roundtable was kindly sponsored by Ferguson Litigation Funding

Published by The Law Society Gazette, 13th March 2017: https://www.lawgazette.co.uk/people/roundtable-litigation-funding/5060204.article