Why Damages-Based Agreements Aren't More Popular

By **Andy Ellis** (September 18, 2020, 4:17 PM EDT)

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Some political commentators have suggested that Boris Johnson's desire to be prime minister was stronger than his willingness to embrace what being prime minister actually entails.

We can each be the judge of that theory, but there is an analogy to be drawn with lawyers and damages-based agreements: The idea seems a lot more attractive than the reality.

For as long as I've been working in litigation costs, sections of the profession have looked enviously at the U.S. model of contingency fees and bemoaned the resilience of the common law principle of champerty that blocks the ability to import that form of fee arrangement into English law.

Exceptions to the common law have been required to take statutory form, hence the successive legislative provisions for conditional fee agreements and, in 2013, for damages-based agreements.

The main problem with either form of agreement is that any form of noncompliance risks rendering the fee agreement unenforceable. Hence, if the statute or accompanying rules are ambiguous, some clients and paying parties are bound to exploit any corridors of uncertainty in the hope that liabilities for costs are avoided. They will and they do.

Add into the mix that the damages-based agreement regulations do not permit hybrid arrangements and require lawyers to risk 100% of their fees, and it is easy to understand why the appetite for taking on meaty commercial cases for a share of the spoils has been far smaller than many predicted. It can work for third-party litigation funders but for lawyers the advantages are by no means clear cut.

One of the first technical challenges to damages-based agreements to reach the court was decided in July in Lexlaw Ltd. v. Zuberi[1] by Judge Nicholas Parfitt. It concerned the ability of the law firm to protect itself against a client terminating the agreement before the end of the case — in this case, a client who goes on to win the case by accepting an improved offer.

A clause in the damages-based agreement required the client to pay fees calculated on an hourly rate basis if the agreement was ended by the client before the outcome of the case had been decided.

The client relied on Paragraph 4 of the Damages-Based Agreement Regulations 2013 to argue that only one form of payment was permissible under the legislation. She argued that to include an alternative method of calculation in any circumstances rendered the agreement unenforceable — even though it was not the clause relied upon by the claimant law firm to seek payment.

The claim was for the agreed percentage fee relative to the proceeds of the litigation, i.e. holding the client to the agreement and contesting the client's right to avoid payment by unilateral termination.

The lack of clarity in the drafting of the regulations had been highlighted previously by editorial comment in the costs and funding supplement to the White Book, in Cook on Costs and in Friston on Costs. It was described by Judge Parfitt as a known issue.

The judge took a purposive interpretation of the legislation and concluded that there cannot have been an intention to preclude lawyers from the form of protection upon unilateral termination by a client. The termination clause was part of a wider agreement with the client.

The issue is still potentially live as the Court of Appeal has given permission to appeal and cautious lawyers are most likely to conclude that it is not yet safe to adopt protective Lexlaw-style termination clauses.

Back in the conditional fee agreement arena, a lot of water has passed under the bridge since the "costs wars" of the early 2000s, which were fueled by the recovery of success fees from paying parties who were motivated to step into the shoes of their opponents and to exploit any aspects of noncompliance with the early iterations of the conditional fee agreement regulations.

The legislative requirements themselves have been progressively simplified. As a result of that simplification, most costs specialists thought that the heat had disappeared from technical arguments around strict compliance. That was until an 80-page judgment by the Senior Courts Costs Office Judge Master Jennifer James was handed down in Global Energy Horizons Corp. v. The Winros Partnership.[2]

The Winros Group, formerly Rosenblatt solicitors, fell out with a client for whom they had acted under a series of three conditional fee agreements. The cause of the relationship breakdown was a significant divergence between expert valuation of the claim commissioned by Winros and the client's own view of potential recovery.

The client proceeded to instruct Bird & Bird to lead the quantum part of the claim. Winros found the position untenable and believed they were being frozen out. Winros terminated the retainer.

The client instructed Eversheds Sutherland to challenge the fees rendered upon termination of the retainer by Winros under Section 70 of the Solicitors Act of 1974.

At the risk of over-condensing a very dense factual matrix, there are effectively only two things that can go wrong with a conditional fee agreement in civil proceedings since the regulations were simplified that would render it in breach of Section 58 of the Courts and Legal Services Act 1990. It could be oral when it is required to be in writing, or it could seek a success fee of more than 100%.

Winros was found to have crossed both those lines. The first involved the failure to commit claimed oral variations to the retainer into writing.

What proved fatal to recovery of costs across all three conditional fee agreements was the possibility that the negotiated minimum payments under the agreements could have resulted in recovery of more than 100% of the base costs.

The fact that this hypothetical breach did not materialize — and by some considerable margin given the vast amount of work carried out — did not alter the finding that the agreements were unenforceable.

The consequences are that Winros cannot recover its costs of some £7.6 million (approximately $9.8 million) or success fees of some £3.4 million and must return the advance costs it had retained; all this despite the acknowledgement of its sterling work over more than six years to obtain a favorable outcome on liability. The costs of the assessment are likely to be enormous.

This decision, in which an appeal is also sought, is a blast from the past, but reminds us that dangers still lurk for all forms of contingent fee agreements when statutory exceptions are what allow them to be enforceable and when there are fuzzy edges around interpretation.

Just as more relaxed regulation of conditional fee agreements did not save Winros, the prospect of damages-based agreement reform later this year might not repair confidence levels in contingency fees.

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[1] Lexlaw Ltd. v. Zuberi [2020] EWHC 1855 (Ch).

[2] Global Energy Horizons Corporation v. The Winros Partnership (2020), 20 August, SCCO (unreported).