Third party funding: a litigation lifeline?

Simon Davenport QC, Daniel Goldblatt & Sergey Litovchenko on finding third party litigation funding in the age of COVID-19

IN BRIEF

▶ How lawyers and their clients can best position themselves to apply for and negotiate third party litigation funding.

As the COVID-19 pandemic and economic fallout drain liquidity from businesses and individuals, self-financing lawsuits will become increasingly challenging. Meanwhile, the litigation finance industry, which has tended to be non-correlated to financial markets or counter-cyclical, is in a position to provide a lifeline. But with so much demand for cash, funders will become more discerning about which cases they back and will charge more for their services.

Third party funding, otherwise known as litigation funding or finance, is the loaning of capital by a fund or investment firm to cover a party's legal costs, which is repayable (with a return) in the event of a successful claim. Put crudely; it is paying for litigation when a party has a good case but either cannot afford or will not fund it themselves. As set out below, applying for third party funding requires careful preparation and investment of a good deal of trust in the relationship between funder and client, which is akin to a partnership: both share the profits, and risks.

This article examines how lawyers and their clients can best position themselves to apply for and negotiate third party litigation funding.

First, we will examine what third-party funding involves, second, how to get it, third, what our experience of applications involving Russian and CIS clients has been, and finally, what the typical costs involve.

Background

Traditionally, claimants paid their own way through disputes. It remains the case that if you have the money available, self-funding is often the cheapest way to litigate. Because the litigation risks are entirely one's own, private funding benefits from avoiding the inconvenience of persuading a financial partner to come on board and their oversight during the stresses of litigating.

Third party funding is just one option amongst an increasingly large range of funding sources which emerged from the unravelling of the medieval English law doctrines of maintenance and champerty, which were aimed at preventing fraudulent and vexatious claims. In *R (Factortame Limited and others) v Secretary of State for Transport, Local Government and the Regions (no.8)* [2002] 3 WLR 1104, Lord Philips MR summarised the doctrines:

> 'A person is guilty of maintenance if he supports litigation in which he has no legitimate concern without just cause or excuse. Champerty occurs when the person maintaining another stipulates for a share of the proceeds of the action or suit.'

As courts have taken the view that without some form of third party funding, many just claims would not be brought, the modern formulation of the doctrines do not carry a criminal sanction and only apply to cases involving an element of impropriety, such as excessive profits or control over the litigation.

Other sources of funding include:

- Conditional fee agreements (CFAs) and damages-based agreements (DBAs), whereby one's lawyers take on some of the litigation's risk;
- Before the Event (BTE) and After the Event (ATE) insurance policies. There are also specialist insurance products such as Directors' and Officers' insurance policies which can assist defending claims brought by shareholders or regulators;
- More recently, crowdfunding through websites such as Crowd Justice has gained in popularity (notably in Brexit-related judicial reviews) although this is still considered a rather unusual funding model and is mainly used for non-commercial cases;
- Another option is 'friendly funding' or 'pure funding', whereby capital is provided by benefactors or from other corporate or charitable entities that do not seek to benefit from the litigation.

How to access third party funding

Funders look for predictability. With this in mind, clients and their lawyers should carefully prepare their applications, ensuring that risks are highlighted and assessed.

It is helpful to consider the following:

- **Facts.** Outline the key facts as well as a chronology and glossary of who's who. Be succinct: funders will be dealing with multiple applications.
- **Evidence**. Provide and summarise the key documents. Settle a non-disclosure agreement with the prospective funder to maintain confidentiality. Where relevant, obtain the views of experts or have experts lined-up. In contrast to predictable cases are those that used to be called 'a hard swearers' ie, an undocumented dispute over who

said what. This has tended to be the case with the litigation of Russian and CIS oligarchs, which is considered further below.

- **Applicable law and jurisdiction.** Set out the applicable law to the claim and highlight any jurisdictional issues. Do not be afraid to include contingency plans.
- **Causes of action.** Funders do not want half-baked legal analysis. They want a clear outline of which parts of a claim are viable and which are not.
- **Limitation.** If limitation is going to be a problem, do not conceal it.
- **Causation and damages.** This needs to be properly considered. Do not exaggerate the expected value of the claim—be realistic.
- **Enforcement.** Set out a strategy for enforcement and share your investigations regarding what assets the Defendant has and where they are located.
- **Human intelligence.** In some instances it might be a good idea to assess how a defendant might react to different stages of the litigation, set out who the key decision-makers are, what their past litigation record is, which lawyers they use and how their lawyers will conduct themselves.
- **Budget.** A budget is not a fixed, binding contract; it is a sensible step in preparing for litigation. Lawyers should be doing this for their clients so there is no reason why it cannot be done for funders. Do not overlook issues like VAT contingency costs events, such as security for costs applications.
- **Practical issues.** These will be linked to many of the points above, and, in addition, one should consider: (i) whether it is appropriate to obtain ATE insurance before approaching a litigation funder;(ii) which disbursements are unavoidable; and (iii) whether sums need ringfencing.

Applying for funding in a considered manner can be a good exercise in itself: it focuses minds and encourages clients and litigators to put in place a detailed campaign plan. By demonstrating to a funder that you have a legal team that has carefully assessed and prepared the funding application, and has set out the steps needed to win, you will be in a strong position to negotiate the costs funding.

Even where a client is using an experienced litigation team, employing a broker's services to obtain funding can be worthwhile. Although it is an extra expense, the most experienced brokers provide market intelligence on which funders to avoid and which are best for particular types of cases at specific times (something many litigators would not be aware of). They can also more than pay their own way when it comes to negotiating the funding arrangement, particularly the waterfall agreement (see below). Importantly, brokers are often useful in managing the relationship between client and funder, which is often tested during the heat of litigation.

The Russian & CIS experience of applying for funding

From experience, some funders are reluctant to fund cases which involve foreign law. This is especially true of cases where a judgment has already been obtained in CIS states or Russia, and the client is seeking recognition of that judgment and enforcement against assets in England.

Below are some of the issues, certainly not unique to Russia or the CIS, which we have found to have hampered applications for funding.

- **Conflicts within a corporate client.** Senior and mid-management can have different agendas and may seek to influence the process of attracting funding or the allocation of budgets.
- **Similarly, the information provided by different levels of corporate management can be inconsistent.** Solicitors, brokers and third-party litigation funders may be provided with different information on the same case, which can lose the trust of all involved.
- **The contracting process in large and state-owned Russian companies can be overly bureaucratic and slow.** Pedantically detailed cost budgets are required, and funding arrangements are required to provide for every eventuality. This is further complicated by the need to have funding arrangements approved at different levels of management, which can lose valuable time where assets are at risk, as well as the funders' enthusiasm.
- **A lack of documentary disclosure.** This may be because a client is unused to English civil procedure rules and wishes to keep their cards close to their chest, or it could be because contractual arrangements had been made verbally.
- **A fear of political influence.** This can be a worry for investors standing behind third party funds.
- **Inordinately high claim values.** These can be a red flag for funders, because high-value claims are certain to be vigorously defended and will require a deep commitment from prospective funders.

These issues add layers of uncertainty to a case which funders (and their investors) shy away from. For the most part, problems like these can be dealt with, providing clients are well advised and well prepared.

The typical costs of funding

In reality, every funding arrangement has its own unique costs determined by several factors including the value of the claim and enforcement issues. That said, the average funding deal is a percentage of the damages awarded or agreed or, alternatively, a multiple of the money invested in the case.

As a rule, the cost of funding gets more expensive the closer you get to trial. That is why it is important for litigation teams and clients to consider third-party funding from the outset and understand what they need to fund, for how long, and what elements of a case are more likely to be met by way of opposition from the other side.

The most overlooked cost to third party funding is the waterfall agreement, which sets out how and in what order the claim proceeds are to be divided between the various entities with a financial interest in the claim i.e. client, funder, lawyers and insurer. The best waterfall agreements align the interests of client and funder, but many do not. Waterfall clauses are a part of funding arrangements which require a lot of thought. Where such an agreement has not been properly considered or badly drafted, it can turn a technically successful litigation outcome very sour, very quickly.

As noted above, a broker can help negotiate down the overall cost of funding, but the key is to ensure an application is carefully prepared and thought through.

Conclusion

There are going to be innumerable disputes that arise out of the current public health and economic crisis. Many will deserve funding, but some will not.

Therefore, it is important to select the right cases and package them well for funders. Third party litigation funders need to be given a sensible analysis of the key issues outlined above, and they need to be shown a clear path through every stage of the litigation process. As with most things in litigation, credibility and preparation are everything. NLJ

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