Litigation funding is not a loan

Litigation funding is 'non-recourse' funding, not a loan. If a case is lost a funder loses its investment and no sum is repayable by the funded party.

Who are third party funders?
Third party funders range from large international funders with over USD500m to invest in disputes, to smaller funders with relatively limited capital. Funders can be hedge funds, be listed on the Alternative Investment Market (“AIM”) in London, and include private equity funds (typically based in Guernsey, the Isle of Man, Jersey and outside England).

What does third party funding cost?
A litigation funder’s fee will typically be a multiple of cash advanced or a percentage of monies recovered, whichever is the greater. Funders are involved with litigation for financial profit only, seeking to maximise return to their investors.

Key issues for a funder:
- Quantum
  - The value of the claim (asset) and what is the potential recovery.
- Merits
  - The probability of a successful outcome and number and types of issues in dispute. Funders only want claims with good prospects of success.
- Recoverability
  - That the opponent is good for the money and there are no potential enforcement issues. Funders are not interested in victories that do not give rise to recovered monies and a return for their investors.

What types of disputes will funders support?
Funders will generally invest in any type of dispute; including court proceedings in England, most forms of domestic and international arbitration, and tribunal proceedings. Save for specialist funders, most funders will not invest in divorce/matrimonial disputes.

Will funders cover paid (retrospective) costs?
Possibly.

Ratio of level of required funding (potential costs) to potential recovered monies
In commercial disputes, most funders generally look for a minimum ratio of 1:8, with some funders looking for a higher potential ratio between the potential costs and the amount of monies that will hopefully be recovered from an opponent. Some smaller funders may for lower value commercial claims consider lower ratios between potential costs and potential monies to be recovered.

Typical funding documentation
- Non Disclosure Agreement or Exclusivity Agreement
  - Some, but not all, want an exclusivity period and non disclosure agreement during due diligence prior to a Funding Agreement being entered into.
- Funding Agreement
  - The terms of funding between the funder and funded party.
- Priorities Agreement
  - In what order the funder, solicitors, legal expenses insurer (if required) and the client are paid in the event of monies being recovered.
- Deed of Assignment
  - Assignment of any legal expenses insurance policy.

Advantages and disadvantages of funding for a client

Advantages: Funding enables a client
- without sufficient funds to pursue a claim with good prospects of success
- with sufficient funds to pursue a claim with good prospects of success without risking its own funds, thereby enabling a client to utilise its own monies elsewhere e.g. to develop its business
- to potentially keep litigation costs “off balance sheet”
- to recover monies from its assets (potential claims).

Disadvantages: The client may or will
- have to agree an exclusivity period, possibly with cancellation terms, for a funder to consider whether to fund, with the risk of funding not being forthcoming or offered on unacceptable terms, and a period of one to two months or more having been lost in dealing with the particular funder
- have to pay a funder and lose a substantial element (e.g. possibly between 20% and 40%) of the monies recovered from an opponent – depending on the multiple of cash advanced or amount of damages recovered, and the fee payable under the funders pricing model

Continued on next page >
Third party funding of litigation

March 2017

- lose an element of control over the conduct of the case
- have to take (e.g. for English court proceedings) after the event (“ATE”) legal expenses insurance, possibly with an ATE insurer proposed by the funder, for any potential costs liability to an opponent
- give up some equity in their property where a funder takes a stake e.g. in intellectual property cases
- remain primarily liable for its solicitors and other costs, and any costs liability to an opponent, irrespective of the funding agreement (e.g. if a funder does not pay, withdraws funding or becomes unable to fund for any reason).

Potential risk and issues for third party funders

- The claim is unsuccessful and funds (i.e. costs) invested are lost
- In English court proceedings, or other forum where costs can be awarded against a non party, the opponent joins the funder to the proceedings and obtains a non party costs order against the funder
- The value of any recoverable damages and/or costs is reduced as a consequence of the opponent’s cross claims, or the claim only gives rise to a low recovery of monies
- The claim is successful but the client is unable to recover damages and/or costs as a consequence of the opponent’s insolvency or enforcement issues.

Litigation finance

Some funders may be willing to provide finance to keep a client’s business trading during the course of litigation, as opposed to actually funding the claim. This is achieved by using the value in the asset (the claim) to provide finance to the business. It may also be possible to use the value of a judgment to finance the cost of opposing an appeal.

Who has money and who are the funders?

In dealing with any potential funder, care must be taken to ensure that you are dealing with a funder who holds funds, as opposed to a broker/intermediary who arranges funding. Also, if you want to have the entire estimated funding secured in a designated account, this may be available – at an additional cost.

Funders and security for costs

If you are required in the course of a dispute to provide security for an opponent’s costs (in the event of the claim failing and the opponent being awarded costs), a funder may finance the costs of a bank bond or other security – at an additional cost.

Litigation risk transfer

Pinsent Masons provides specialist advice on litigation risk transfer options.

For further information please contact:

Keith Levene
Legal Director (Cost Lawyer)
London
T: +44 (0)20 7490 6205
M: +44 (0)7770 350568
E: keith.levene@pinsentmasons.com

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