Litigation funders respond to US calls for increased regulation

Edward Machin - Friday, 03 February 2012 13:26

UK litigation funders have come out fighting after a prominent US lobby group's claims that third-party funding should be "discouraged at all costs." Teething pains or something more ominous for the burgeoning industry? *Edward Machin* considers the fallout.

But it was going so well for UK third-party funding: a voluntary Code of Conduct, launched in November by Lord Justice Jackson, has been praised by the judiciary, funders and commentators alike as representing, in the words of one practitioner, "the Magna Carta of litigation funding."

Heartening as they may have been, such platitudes have not stopped the industry coming under attack from the Chamber Institute for Legal Reform (ILR), a Washington, DC-headquartered advocacy group affiliated with the US Chamber of Commerce, which recently issued a vicious rebuke of the nascent Code while further claiming that litigation funding "should be discouraged in all circumstances."

Led by its president, Lisa Rickard, the ILR is seeking to rip UK litigation finance from its roots, calling the Code "inadequate" and one which "does not address the risks and concerns about litigation funding raised by Lord Justice Jackson in his review of civil litigation costs."

The report continued: "The Code contains a number of troubling provisions that would tolerate, if not promote, funding misconduct and incentivise lawsuit abuse; [it] does not address the unique dangers posed by litigation funding in collective proceedings; and does not contain adequate safeguards against litigation abuse."

Unlikely as this is to become reality, however, the ILR alternatively calls for the Code to be replaced – or supplemented with – a "robust regulatory regime" and statutory safeguards that "discourage litigation abuse by raising the cost of, or reducing the potential return from, unethical or improper behaviour by litigation funders."

Meanwhile, a report authored by academics at the universities of Oxford and Lincoln has found that while the UK market remains ripe for commercial litigation funding, effective regulation may soon come to play a prominent role in the industry's wider success.

Having interviewed nineteen prominent funders both in Britain and further afield, the 158-page study – *Litigation Funding: Status and Issues* – contrasts the UK experience with those of the USA, Austria and Germany, Canada and Australia to offer arguably the most comprehensive overview of current global funding practices to date.

Focusing primarily on the UK and its recently-launched Code of Conduct, the report's analysis bears out the fact that a full statutory code may well be inevitable – while simultaneously raising concerns around damages-based agreements.

"We recommend that funders should not control tactical decisions in litigation," the report concludes, "and that the demarcation of roles between client, lawyer and funder should remain and should be set out clearly in professional ethical requirements."

Head of the Centre for Socio-Legal Studies at Oxford University and co-author of the study, Professor Christopher Hodges, says third-party funders ought to be kept at arm's length during the litigation process, for two reasons.

First, he highlights the danger that funders "might opt for a lower settlement than the client might want in order to resolve a case quickly," while also warning of the perils of the funder and lawyer's firm colluding against their client's best interests.

"This does not appear to have happened yet in the UK, but we want to ensure that any risk of it happening in the future is removed," says Hodges. "Clients need more legal protection as otherwise there is potential for third-party funders to control claimants' cases for their own advantage."

Hodges' co-author, Dr Angus Nurse, says that as new firms enter the UK litigation funding market, as continues to be the case, a resultant increase in available capital "may dictate a review of funding regulation to achieve both client protection and protection of the funding market itself."

He adds: "As a result, we consider that self-regulation may not be sustainable in the long term."

Scévole de Cazotte, vice president of International Initiatives at the ILR, says his organisation's attitudes to ligitation funding stem from the US litigation system being increasingly "riddled with abuses and problems that are generally associated with the influx or interest people have in putting money in lawsuits."

He explains: "We're worried about third-party litigation funding because it's very reminiscent of that fundamental tenet of investing in lawsuits. It's the idea that you can make money from litigation, and with litigation finance it's no longer just a law firm or lawyers investing – you suddenly have hedge funds or very large investments interests coming into the litigation sphere."

According to de Cazotte, previously a regulatory lawyer at WilmerHale in Washington, DC, "we're not saying the problems are there yet, but they will happen, for sure. Increasingly you will hear more voices expressing their concerns about the need for a statutory framework that would put into place safeguards that would prevent the problems we're talking about."

Central to the ILR's disquiet is its perception of a growth in firms looking to fund consumer claims – a practice already established in Australia and which de Cazotte expects to blossom in the UK, given the model's inherent profitability. "Based on our experience and observation of other markets, it's safe to say that this is something that will produce problems," he says.

"It will be a good thing, a safe thing, to prevent it ahead of time with safeguards, because once the genie is out of the box it's very hard to put it back in."

Pot, meet kettle

Leslie Perrin, chairman of Calunius Capital, a London-based litigation funder, is first up to contest the ILR's document.

"You've got to remember that the US Chamber of Commerce is the mouthpiece for Big Business," he begins, "and quite why it is committing so much time to lobbying for changes to the law in the UK is certainly a question to be asked."

According to Perrin, formerly head of litigation and a senior partner at Osborne Clarke, "the ILR should actually be called the 'Institute for the Prevention of Legal Reform,' because it's one of those oxymoronic institutions that does exactly the opposite of what it says on the tin. They are notorious in trying to clamp down on access to justice, and have been trying to have litigation finance banned in any form in certain US states."

He adds: "The US Chamber of Commerce is the largest lobbying organisation in the entire world, and they want to preserve the in-built advantage that their members have in litigation, when they have breached their contracts with economically weaker counterparties."

Argentum Litigation Services chief executive Louis Young is similarly scathing in his assessment of the ILR's report. "It's a reasonably well written document," says Young, whose firm launched on AIM in 2009, "but it just seems that they've taken a little bit of sugar and fluffed it up into a candy floss on a stick and they're now waving it around."

Young points to one ILR statement in particular, concerning the percentage of a litigation recovery that a funder may obtain, which, it says, "should be relatively low to ensure that litigation remains a mechanism to redress grievances – rather than an investment tool for disinterested profit-seekers."

"That's absolute rubbish," says Young, "particularly coming from an organisation like the US Chamber of Commerce. They represent possibly the pinnacle of capitalism on a global basis, and then they make a statement like that; it's incredible."

With the US Chamber in mind, the story took a particularly interesting turn on Wednesday (1 February), in the form of a House of Lords debate on the Legal Aid, Sentencing and Punishment of Offenders Bill, currently at committee stage.

A numbers of amendments to Clause 53 of the Bill, tabled by Lord Thomas of Gresford, seek to restrict UK litigation funding and impose statutory regulation on those in the industry.

Perrin, who also serves as chairman of the Association of Litigation Funders, launched on the same night – 23 November 2011 – as the Code of Conduct, says there's more to things than meet the eye, however.

"The US Chamber of Commerce seems to have persuaded Lord Thomas to table the amendments to the Bill," he explains.

"The Association was set up on 23 November – an interesting date indeed, given that the US Chamber managed to get its amendment onto the draft Bill on the very same day; that's no accident."

Happy days?

Founder of Therium Capital, Neil Purslow, says the UK third-party funding industry has never shied away from effective regulation, nor high standards to it hold itself to.

"We want a proper funding industry," he explains. "One lawyers will be comfortable recommending to their clients, and their clients will be comfortable taking funding from. There's no agenda here to avoid proper regulation – it's simply not in our interests to do that."

Like Calunius' Leslie Perrin, Purslow remains somewhat nonplussed by the ILR's report, while noting that the Oxford-Lincoln study similarly "hasn't identified any examples of abuse or problematic behaviour as yet, so we're talking about something that is a fear about what may happen in the future."

Purslow accepts that the Code doesn't purport to regulate every possible permutation raised by litigation funding. Nonetheless, he says, we're currently looking at a small – but growing – industry, one in which there currently "isn't any appetite for people to provide statutory regulation, and all the costs that come along with that for what is still a nascent industry."

He adds: "The Code is a very British, pragmatic solution to the issue of regulation, and it's excellent for that. Lord Justice Jackson's happy; the Master of the Rolls is happy, as are the funders, the insurers, Mike Napier and the Civil Justice Council.

"All of those people are happy, so it seems odd that the US institute is unhappy about it, and sees fit to tell us that we need to have a different form of regulation when all the major stakeholders here feel we've struck the right balance."

Argentum's Louis Young speaks for the majority of funders operating in the UK when he says that "we, for one, are not disinterested profit seekers. We are professional investors who carry out extensive due diligence into the matters we invest into."

He goes on to explain that it is not in the interest of funders to promote unmeritorious claims, given that "we, like any investor in any asset class, look to back successful opportunities, not spurious and frivolous claims which is one of the underlying premises that the ILR appear to have based their article on."

Fulbrook Management's Selvyn Seidel, one of the industry's elder statesmen, having also co-founded funding giant Burford Group, has the final word.

"No-one is saying the industry is perfect," he says, "and no-one is saying the new UK Code is perfect, either."

On the other hand, Seidel remarks, "how can anyone say that there is not real room for real benefits from the industry, provided the participants have quality and integrity, and the market see value, wanting the product and the services?"

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