

**LITIGATION FUNDING:
ITS PLACE IN THE CIVIL JUSTICE SYSTEM**

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ABSTRACT

The practice of third parties funding litigation for commercial purposes was, for centuries, impermissible, owing to the operation of the doctrines of maintenance and champerty. But it is now permissible in England and Australia, and accepted as part of the legal landscape. The change in the court's attitude was largely driven by a pragmatic desire to improve access to justice for the impecunious.

The question motivating this thesis is: where does litigation funding fit in the modern civil justice system?

This thesis has three objectives. The first is to assess critically the various criticisms that are made of litigation funding (such as concern about the prospect of third-party control of litigation, or the commodification of legal claims). These criticisms – which are the vestiges of the doctrines of maintenance and champerty – can be seen as reflecting a particular concept of the proper role and values of the civil justice system. But recent decades have seen enormous changes in the civil justice system and the legal profession – including the acceptance (or imposition) of managerial culture, and market rhetoric. When one considers the values and priorities of the modern civil justice system, it can be seen that commercial third-party litigation funding is a consistent part of the broader picture.

Secondly, the thesis presents a more nuanced account of how litigation funding promotes 'access to justice': namely, that it removes or mitigates a variety of disincentives to litigation (which deter all rational litigants, and not just the impecunious).

Finally, the thesis identifies market failures which might exist or emerge in the litigation funding market, identifies some difficulties in the current state of regulation

in England and Australia, and make some broad suggestions for regulatory options. The task of regulation ought to be informed by the conclusions reached in the first parts of the thesis.

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To Adam, Alice and Laura, with love and thanks

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TABLE OF ABBREVIATIONS

ALF	Association of Litigation Funders
ALF Code	Association of Litigation Funders, Code of Conduct for Litigation Funders
ALFA	Association of Litigation Funders of Australia
ALFA Guidelines	Association of Litigation Funders of Australia, Best Practice Guidelines for Litigation Funders and Managers
ALRC	Australian Law Reform Commission
<i>Arkin</i>	<i>Arkin v Borchard Lines (Nos 2 and 3)</i> [2005] EWCA Civ 655; [2005] 1 WLR 3055
ATE insurance	After the Event insurance
FCA	Financial Conduct Authority
FSA	Financial Services Authority
<i>Fostif</i>	<i>Campbells Cash and Carry Pty Limited v Fostif Pty Limited</i> (2006) 229 CLR 386
LASPO	Legal Aid, Sentencing and Punishment of Offenders (LASPO) Act 2012 (UK)
PRA	Prudential Regulation Authority

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CHAPTER 1 – INTRODUCTION

Commercial litigation funding is an emerging and relatively recent phenomenon in civil justice. It typically entails a third party paying for the legal costs of a claimant, in exchange for a percentage share in the proceeds in the event of a favourable judgment or settlement. The claimant bears no liability for their own legal costs even in the event that the litigation is unsuccessful; the risk of adverse costs may be dealt with by insurance, or may be borne by the claimant or the funder.

The utility of such arrangements is obvious. Litigation is notoriously expensive, and government-funded legal aid has become virtually extinct. As a result, there is a perennial difficulty in ensuring that putative litigants are able to access the services of lawyers, and to litigate. A variety of market and regulatory responses may be observed, including the introduction of alternative fee agreements, costs management by the court, and after-the-event insurance for legal costs. None of these solutions, by itself, is a panacea.

For the impecunious, or a class action claimant, commercial litigation funding may enable a claim to be brought where it would otherwise lay dormant. But even a well-resourced claimant may benefit from transferring to an external funder the high and unpredictable cost of litigation. Users of litigation funding are diverse, including insolvency practitioners, class action claimants and large companies.

The place of litigation funding in the civil justice system is, however, unsettled. For centuries, the doctrines of maintenance and champerty prohibited third parties from paying for a litigant's legal costs. These doctrines had their genesis in the vastly different environment of mediaeval England, where litigation was used oppressively,

and courts were unable to curb abuses of process. Over time, the doctrines of maintenance and champerty have been whittled away by various exceptions, and it is now clear – in England and Australia, at least – that litigation funding is usually permissible. In reaching this conclusion, courts were driven by pragmatism: the recognition that litigation funding provided one solution to the intractable problems of access to justice.

But important questions remain, and it is the task of this thesis to address those.

First, one may still see in the jurisprudence and commentary on funding vestiges of the concerns which underpinned the doctrines of maintenance and champerty. It remains relatively commonplace to see suggestions that litigation funding might undesirably stir up litigation where it would otherwise not be brought, or that it involves undesirable commodification of claims, or of the legal profession. One response is to point – as courts have done – to the countervailing ‘access to justice’ benefits. But in this thesis, I adopt a different approach. I assess the various policy grounds which underpinned maintenance and champerty (and continue to underpin criticism of litigation funding), and conclude that they are largely misplaced in the modern civil justice system. When one considers the values and priorities of the modern civil justice system, one can conclude that commercial third-party litigation funding is a consistent part of the broader picture. In chapter 2, I consider the history of maintenance and champerty, and its modern application to litigation funding, identifying the vestiges of the policy concerns which remain. In chapters 3 to 5, I explain why those policy concerns are misplaced in the modern civil justice system. In chapters 6 and 7, I examine the state of the modern litigation funding market, and propose how we might accurately characterise the role of litigation funding in facilitating access to justice.

Secondly, the regulation of litigation funding has been piecemeal and unsatisfactory. In England and Australia, there is a patchwork of voluntary self-regulation, regulation by the court in the form of evolving jurisprudence, and, in Australia, some limited government regulation. Regulation by courts is inherently uncertain and retrospective; voluntary self-regulation is limited in its ability to guide the market; and the externally-imposed regulation has been adventitious and reactive. In chapter 8, I consider the market failures which might emerge (or already exist) in the market for litigation funding. In chapter 9, I address the current state of regulation. In chapters 10 and 11, I identify some broad parameters for how litigation funding might be regulated.

This thesis focuses on the position in England and Australia. The civil justice system in these jurisdictions shares a common history, and litigation funding is well-established in each, but the progress of litigation funding law and practice in each has been quite different, enabling some valuable contrasts and comparisons. However, litigation funding is emerging throughout the common law world – with varying degrees of acceptance in different jurisdictions – and much of this thesis will be applicable beyond England and Australia.

I have sought to reflect the state of the law as at March 2020, although occasional reference has been made to changes which have been proposed after that date.

CHAPTER 2 – MAINTENANCE, CHAMPERTY AND LITIGATION FUNDING

For centuries, it was impermissible for a third party to fund litigation, owing to the doctrines of maintenance and champerty. In this chapter, I explain the historical origins of these doctrines, and how they have been attenuated over time in the interests of facilitating access to justice. I also identify how the vestiges of maintenance and champerty continue to set the outer limits of permissible funding agreements in England and Australia.

History of maintenance and champerty

Many definitions of maintenance and champerty have been given over the centuries as the law has evolved.¹ Maintenance is assisting in another party's lawsuit, in circumstances where the maintainer has no interest. Champerty is a more serious form of the same conduct: it entails assistance (including financial assistance) which is rendered for the purpose of sharing in the proceeds of the litigation. Until recently, maintenance and champerty were crimes and torts in England and Australia.

Mediaeval origins

The doctrines of maintenance and champerty have their origins in medieval England. It was a time during which courts were relatively weak, and unable to prevent abuses of process. Wealthy and powerful barons were able to manipulate courts. Maintenance was one of the means by which they did so.

¹ *Bradlaugh v Newdegate* (1883) 11 QBD 1 (HC), 5-6. But cf Percy Henry Winfield, *History of Conspiracy and Abuse of Legal Procedure* (Cambridge University Press 1921), 131-8, who discusses different forms of maintenance which existed at an earlier stage of the law's development.

The practice of maintenance took place in a broader context of other behaviour aimed at increasing the landholdings of the barons.² It was not uncommon for powerful barons simply to seize land by force. If the true owner went to court to seek justice, he would be disappointed: judges would be reluctant to deliver judgment against a powerful baron. Their power and influence was sometimes demonstrated through presence at court, or even through bribery or displays of force.³

From this practice, other abusive practices developed. The success of the barons in court did not escape the attention of others who desired other's land but did not, themselves, have the might to secure it. For a litigant, it was cheaper to seek the assistance of barons than to engage a lawyer. The barons would benefit from gaining rights of patronage over those they assisted, or a share of the proceeds.⁴ Maintenance became so prevalent that 'the maintainer became one of the recognised retainers of the barons and had his own special livery.'⁵ In time, even 'Churchmen... and ladies of the Court' came to engage in maintenance.⁶

To curb the abuses of maintenance and champerty, statutes were enacted which imposed penalties on the practices.⁷ The legislation which banned maintenance was

² Max Radin, 'Maintenance by Champerty' (1936) 24 California Law Review 48, 64.

³ AH Dennis, 'The Law of Maintenance and Champerty' (1890) 6 Law Quarterly Review 169, 173; Edmond H Bodkin, *Maintenance and Champerty* (Stevens and Sons Limited 1935), 1.

⁴ Bodkin (n 3) 2.

⁵ *ibid.*

⁶ *ibid* 3. See also Percy H Winfield, 'The History of Maintenance and Champerty' (1919) 35 Law Quarterly Review 50, 68; Winfield, *History of Conspiracy and Abuse of Legal Procedure* (n 1) 154-5.

⁷ Winfield, 'The History of Maintenance and Champerty' (n 6) 59-68; Winfield, *History of Conspiracy and Abuse of Legal Procedure* (n 1) 142-60; Sir William Holdsworth, *History of English Law*, vol III (5th edn, Sweet and Maxwell 1942), 394-400 each provide a detailed history of the various statutes. See also Dennis (n 3) 170-3, 174. Champerty was a crime at common law: Winfield, 'The History of Maintenance and Champerty' (n 6) 57-8; Winfield, *History of Conspiracy and Abuse of Legal Procedure* (n 1) 138-41; Bodkin (n 3) 3. It seems that the torts of both champerty and maintenance were created by statute: Winfield, 'The History of Maintenance and Champerty' (n 6) 57-9; Bodkin (n 3) 3.

primarily concerned with preventing corruption of the judiciary,⁸ in an era when the courts were insufficiently equipped to protect against abuses. The law was⁹

... originally directed rather against the perversion of justice by bribery or by actual or threatened violence than the pecuniary damage caused to a party by the stirring up of speculative litigation for which the plaintiff was unable to pay...

Maintenance and champerty proved difficult to eradicate because, as Winfield notes, 'No branch of the law depended more for its efficacy on the uprightness of those who were called upon to enforce it.'¹⁰ Those who engaged in maintenance and champerty included the rich or powerful, including judges and government officials.¹¹ It was necessary to increase the penalties to deter the practices, and it was not until the Tudor period that it was truly curtailed.¹²

Thus, the primary purpose of the prohibitions against maintenance and champerty was to protect the courts from conduct which today would be clear abuses of process. They were directed at preventing judicial corruption. The doctrines also protected defendants from the unscrupulous behaviour of maintainers, and the oppression caused by litigation, but this was secondary.

There was another explanation for the aversion to the practices of maintenance and champerty. Prevailing Christian doctrine taught that litigation was to be avoided, and that it was desirable that debts be forgiven.¹³ Although a claimant might be required to litigate as a last resort on his own behalf, the involvement of a third party 'was not

⁸ Dennis (n 3) 173; Bodkin (n 3) 5.

⁹ Bodkin (n 3) 5.

¹⁰ Winfield, 'The History of Maintenance and Champerty' (n 6) 68; Winfield, *History of Conspiracy and Abuse of Legal Procedure* (n 1) 154.

¹¹ Dennis (n 3) 170-1; Winfield, 'The History of Maintenance and Champerty' (n 6) 68.

¹² Winfield, 'The History of Maintenance and Champerty' (n 6) 71; Bodkin (n 3) 3-4.

¹³ Radin (n 2) 56, 58.

public spirit, but dangerous officiousness, likely to be based on the worst possible motives'.¹⁴ There was no sense of a public duty amongst citizens to assist the cause of justice.¹⁵

At its zenith, the law of maintenance was extremely wide. For example, it was maintenance to give evidence otherwise than under subpoena, or to express publicly an intention to provide financial support to a party to litigation, or to encourage counsel to act pro bono.¹⁶

Erosion of the doctrines in the 19th century

The harshness of the restrictions led to the recognition of numerous categories of exception.¹⁷ The exceptions arose where the maintainer had:¹⁸

an actual valuable interest in the result of the suit itself, either present, or contingent, or future, or the interest which consanguinity or affinity to the suitor give to the man who aids him, or the interest arising from the connection of the parties...

The court would treat maintenance as justified if the maintainer and the party to the litigation shared a recognised relationship. The relationships included master and servant (either could maintain the other),¹⁹ 'a fellow commoner defending rights of common', 'a landlord defending his tenant in a suit for tithes',²⁰ or 'an heir-at-law maintain[ing] the title of the person in possession'.²¹ Maintenance arising from

¹⁴ *ibid* 58. See also *Dennis* (n 3) 173, 174-5.

¹⁵ *Radin* (n 2) 58.

¹⁶ *Dennis* (n 3) 175; *Bodkin* (n 3) 4.

¹⁷ *Dennis* (n 3) 175-6. See also *Master v Miller* (1791) 4 TR 320, 340; 100 ER 1042, 1053.

¹⁸ *Bradlaugh* (n 1) 11; see also *Dennis* (n 3) 176.

¹⁹ *Dennis* (n 3) 177-8.

²⁰ *Bradlaugh* (n 1) 11.

²¹ *Alabaster v Harness* [1895] 1 QB 339 (CA), 346 (Rigby LJ).

charitable motives – ‘a rich man giving money to a poor man out of charity to maintain a right which he would otherwise lose’²² – was also permissible.

Whatever policy reasons had motivated the development of these exceptions, it seems that by the end of the 19th century, these were treated as rigid factual categories, rather than instances of a broader principle.²³

Secondly, maintenance could be justified if the maintainer and the party shared a common interest in the litigation. This seems initially to have been interpreted quite narrowly, as a legal interest in the very action. Thus, a company which had employed an expert to report upon its products had no common interest with the expert in an action for libel against a newspaper which criticised the report and cast aspersions on the expert’s qualifications and conduct.²⁴ It was determinative that the legal elements of the action for libel were personal to the expert.²⁵ However, as will be seen, the common interest came to be treated more liberally later in the twentieth century.

The original rationales for the doctrines – avoiding abuses of process, and keeping litigiousness in check – continued to be referred to. The risk of abuse of process was given greater emphasis in cases of champerty, with courts referring to the risk that the third party would be tempted to abuse court process by the prospect of

²² *Bradlaugh* (n 1) 11.

²³ *Alabaster* (n 21) 343 (Lord Esher MR), 344 (Lopes LJ), 345-6 (Rigby LJ); *British Cash and Parcel Conveyors Limited v Lamson Store Service Company Limited* [1908] 1 KB 1006 (CA), 1014 (Fletcher Moulton LJ). But see *ibid*, where Lord Coleridge sought to identify some common features of the circumstances in which maintenance would be justified.

²⁴ *Alabaster* (n 21); this was followed in *Oram v Hutt* [1914] 1 Ch 98 (CA).

²⁵ *Alabaster* (n 21) 343 (Lord Esher MR), 344 (Lopes LJ). See also *Oram* (n 24) 104-5 (Lord Parker), 106-7 (Lord Summer).

sharing in the proceeds.²⁶ But reference continued to be made to the idea that litigation was a practice to be avoided.²⁷

All our cases of maintenance and champerty are founded on the principle that no encouragement should be given to litigation by the introduction of parties to enforce those rights which others are not disposed to enforce.

By the late 19th century, it was recognised that champerty had become a doctrine which operated to the detriment of the impecunious²⁸ – unlike its mediaeval ancestor.²⁹

Development of the law in the 20th century

By the early 20th century,³⁰ it was recognised that maintenance and champerty were falling into obsolescence and irrelevance, and that public policy had changed. The doctrine of maintenance had been carved out by numerous exceptions, and the principles were rarely seen in their tortious and criminal forms. In 1908, Fletcher Moulton LJ observed that the doctrine of maintenance was based on law and public policy which was ‘radically different’ to the present day, and that it had been ‘made serviceable’ by a wide variety of miscellaneous exceptions.³¹ His Lordship recognised – in an often-quoted passage – that maintenance in the modern law was³²

... directed against wanton and officious intermeddling with the disputes of others in which the defendant has no interest whatever, and where the

²⁶ *Stanley, Administratrix of Thomas Stanley v Jones* (1831) 7 Bingham 369; 131 ER 143, 146-7; *Guy v Churchill* (1888) 40 Ch D 481, 488; *In re Treppca Mines Ltd (No 2)* [1963] 1 Ch 199 (CA), 219-20; *Giles v Thompson* [1994] 1 AC 142 (HL), 153; *Dennis* (n 3) 170-1, 3.

²⁷ *Prosser v Edmonds* 1 Y & C 481, 497; see also *Harris v Brisco* (1886) 17 QBD 504, 505-6 per Wills J.

²⁸ *Dennis* (n 3) 169, and see generally 176-85 as to the state of the law at the end of the 19th century.

²⁹ *Radin* (n 2) 66; see also 77-8.

³⁰ See, eg *Bradlaugh* (n 1) 7, 11.

³¹ *British Cash and Parcel Conveyors* (n 23) 1013-14.

³² *ibid* 1014.

assistance he renders to the one or the other party is without justification or excuse.

But he remarked, too, that it was ‘far easier to say what is not maintenance than to say what is maintenance’.³³

Fletcher Moulton LJ’s comments became even more accurate as the twentieth century progressed. The introduction of legal aid for civil proceedings, and the development of the practice of trade unions funding claims brought by members against their employers, expanded the range of externally-funded litigation beyond the traditional exceptions. In 1968, Lord Denning MR remarked that:³⁴

Much maintenance is considered justifiable today which would in 1914 have been considered obnoxious. Most of the actions in our courts are supported by some association or other, or by the state itself. Comparatively few litigants bring suits, or defend them, at their own expense. Most claims by workmen against their employers are paid for by a trade union. Most defences of motorists are paid for by insurance companies. This is perfectly justifiable and is accepted by everyone as lawful, provided always that the one who supports the litigation, if it fails, pays the costs of the other side.

It was also increasingly recognised that maintenance and champerty had the potential to operate oppressively, by preventing the impecunious from seeking funds for litigation.³⁵

In 1966, the Law Commission described the crimes as ‘a dead letter in our law’, which had fallen into disuse.³⁶ They noted, too, that the scope of the tort of maintenance

³³ *ibid* 1014.

³⁴ *Hill v Archbold* [1968] 1 QB 686 (CA), 695.

³⁵ *Martell v Consett Iron Co Ld* [1955] Ch 363, 386.

³⁶ The Law Commission, *Proposals for Reform of the Law Relating to Maintenance and Champerty* (1966) [7].

was unclear,³⁷ and that damage was difficult to prove.³⁸ Significantly, the Commission observed that, owing to the support given to litigants by insurers, trade unions and legal aid, ‘the great bulk of the litigation which engages our courts is maintained from the sources of others, including the state, who have no direct interest in its outcome but who are regarded by society as being fully justified in maintaining it’.³⁹ Accordingly, the Commission recommended the abolition of both ‘the ancient and unused misdemeanours and the ancient and virtually useless torts’.⁴⁰ In 1967, this recommendation was effected.⁴¹

The Law Commission did, however, observe that champertous agreements by solicitors were still regarded as contrary to public policy,⁴² as reflected in case law and modern statutes and conduct rules concerning solicitors’ professional obligations – in particular, the prohibition against contingency fees.⁴³ For that reason, the Commission recommended that the rule of public policy in relation to champertous agreements ought to be retained,⁴⁴ and thus the legislation provided that the abolition of the crimes and torts ‘shall not affect any rule of that law as to the cases in which a contract is to be treated as contrary to public policy or otherwise illegal’.⁴⁵ It is not clear whether the

³⁷ In particular, as to the requirement that maintenance occur *without lawful justification* – see *ibid* [10].

³⁸ *ibid* [11].

³⁹ *ibid* [12]-[15].

⁴⁰ *ibid* [19]-[20].

⁴¹ Criminal Law Act 1967 (UK), s 14(1).

⁴² Common interest, consanguinity and charity were never exceptions to the doctrine of champerty: *Bodkin* (n 3) 44.

⁴³ The Law Commission (n 36) [16]-[18].

⁴⁴ *ibid* [20(3)].

⁴⁵ Criminal Law Act 1967 (UK), s 14(2).

Commission intended that the retained rule of public policy would apply only to solicitors,⁴⁶ but, as will be seen, the rule operates more broadly.

In the 1990s, the doctrines experienced a renaissance with the advent of alternative financing arrangements.

The application of the doctrines to litigation investment

The first significant case to consider the application of maintenance and champerty to arrangements which shared many features of modern litigation funding was *Giles v Thompson*.⁴⁷

Lord Mustill observed that the doctrines of maintenance and champerty had their origins in a justice system far removed from modern courts,⁴⁸ but nevertheless considered that ‘the law on maintenance and champerty can best be kept in forward motion by looking to its origins as a principle of public policy designed to protect the purity of justice and the interests of vulnerable litigants’.⁴⁹ The test for identifying maintenance and champerty was that set out by Fletcher Moulton LJ at the turn of the century:⁵⁰

... all the aspects of the transaction should be taken together for the purpose of considering the single question whether ... there is wanton and officious intermeddling with the disputes of others in where the meddler has no interest whatever, and where the assistance he renders to one or the other party is without justification or excuse.

⁴⁶ See The Law Commission (n 36) [16]-[18], but cf [20(3)] and [19].

⁴⁷ *Giles* (n 26).

⁴⁸ *ibid* 153.

⁴⁹ *ibid* 164.

⁵⁰ *ibid*; see also *Thai Trading Co v Taylor* [1998] QB 781 (CA), 786.

The leading modern case on the principles to be applied in determining whether a contract is void for maintenance or champerty is *Factortame*.⁵¹ A firm of accountants had agreed to act on a contingency basis for a group of impecunious claimants who had already succeeded on the question of liability, but required expert evidence to establish the quantum of their loss. The firm retained the necessary external experts, and carried out work, such as document collation, that might otherwise have been carried out by the solicitors.

Lord Phillips MR, who delivered the judgment of the Court, set out the test in the following broad terms:⁵²

in any individual case, it is necessary to look at the agreement under attack in order to see whether it tends to conflict with existing public policy that is directed to protecting the due administration of justice with particular regard to the interests of the defendant

This broad test has continued to be applied.⁵³ The present position is, therefore, that agreements to assist in litigation for a share in any proceeds are, prima facie, permissible and enforceable.⁵⁴ However, the doctrines of maintenance and champerty – in their attenuated form – continue to set the outer bounds of what is permissible. These rules have been said to be ‘primarily concerned with the protection of the integrity of the litigation process in this jurisdiction.’⁵⁵ In general terms,⁵⁶

in considering whether an agreement is unlawful on grounds of maintenance or champerty, the question is whether the agreement has a

⁵¹ *Factortame Ltd v Secretary of State for Transport, Local Government and the Regions (No 8)* [2002] EWCA Civ 932; [2003] QB 381.

⁵² *ibid* [44].

⁵³ See, eg, *Papera Traders Co Ltd v Hyundai (Merchant) Marine Co Ltd (The 'Eurasian Dream') (No 2)* [2002] EWHC 2130 (Comm); [2002] 2 Lloyd's Law Report 692, [43].

⁵⁴ *London & Regional (St George's Court) Ltd v Ministry of Defence* [2008] EWHC 526, [103(a) and (c)].

⁵⁵ *ibid* [103(d)].

⁵⁶ *ibid* [103(b)].

tendency to corrupt public justice and ... such a question requires the closest attention to the nature and surrounding circumstance of a particular agreement.

Whether an agreement is void for maintenance or champerty is highly contingent on the facts of the case at bar. For example, in *Factortame*, it was highly relevant that the firm was not providing expert evidence – in that case, it would have had an interest in the outcome which would have imperilled the necessary objectivity of an expert.⁵⁷ It was also relevant that the claim for liability had already succeeded,⁵⁸ the percentage share was relatively modest (8%),⁵⁹ the firm was reputable and subject to professional regulation,⁶⁰ and counsel and solicitors were involved, who continued to control the litigation.⁶¹

The test in *Factortame* was expressed in terms that directed the court's attention to the tendency of the *agreement*. However, subsequent courts have looked beyond the agreement to other facts, to determine whether the circumstances as a whole indicate that the interests of justice are jeopardised.⁶²

Maintenance and champerty in Australia

Australian courts and legislatures⁶³ have proceeded on the basis that the law of maintenance and champerty is part of the Australian common law. Statutory modifications to the principles of maintenance and champerty have been made in some

⁵⁷ *Factortame* (n 51) [73].

⁵⁸ *ibid* [81].

⁵⁹ *ibid* [85].

⁶⁰ *ibid* [87].

⁶¹ *ibid* [90].

⁶² See, eg, *Papera Traders* (n 53) [45].

⁶³ As noted in *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* [2006] HCA 41; (2006) 229 CLR 386, the abolition acts were premised on the assumption that the principles existed in Australian law, and had a common law – rather than statutory – basis.

states. Statutory reform has substantially reflected the 1967 English Act. In New South Wales,⁶⁴ Victoria⁶⁵ and South Australia,⁶⁶ maintenance and champerty have been abolished as crimes and torts. In each state the rule of law pursuant to which contracts could be set aside as contrary to public policy or illegal has been preserved.⁶⁷ The remaining states – Western Australia, Queensland, and Tasmania – have not enacted legislation altering the common law position. In Queensland, it has recently been held that the crimes (but not the torts) have been abolished, and that the legislation enabling class actions in that jurisdiction has made litigation funding permissible in that context.⁶⁸

In 1960, the High Court identified, as a question for future consideration, the possibility that maintenance and champerty had fallen into obsolescence as common law offences.⁶⁹ A 2006 discussion paper prepared by the Standing Committee of Attorneys-General expressed the view that this was likely the case.⁷⁰ However, in the leading judgment of *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* (*'Fostif'*),⁷¹ a majority of the High Court again left open the position in these jurisdictions.⁷²

⁶⁴ Maintenance, Champerty and Barratry Abolition Act 1993 No 88 (NSW), ss 3 and 4. See also Crimes Act 1900 No 40 (NSW), Schedule 3, s 5; Civil Liability Act 2002 No 22 (NSW), Schedule 2, s 2.

⁶⁵ Abolition of Obsolete Offences Act (Vic), sub-ss 2(2) and (4). See also Wrongs Act 1958 (Vic), s 32 and Crimes Act 1958 (Vic), s 322A.

⁶⁶ Statutes Amendment and Repeal (Public Offences) Act (SA), s 10 and Schedule. See also Criminal Law Consolidation Act 1935 (SA), Schedule 11, ss 1(3) and 3(1).

⁶⁷ Criminal Law Consolidation Act 1935 (SA), Schedule 11, sub-ss 3(2)(b) and (c); Wrongs Act 1958 (Vic), s 32(2); Civil Liability Act 2002 No 22 (NSW), Schedule 2, s 2(2).

⁶⁸ *Murphy & Ors v Gladstone Ports Corporation Ltd (No 4)* [2019] QSC 228.

⁶⁹ *Clyne v New South Wales Bar Association* (1960) 104 CLR 186, 203.

⁷⁰ Standing Committee of Attorneys-General, *Litigation Funding in Australia: Discussion Paper* (2006), 5.

⁷¹ (2006) 229 CLR 386.

⁷² *ibid* [85].

Current state of the law

The plurality in *Fostif* provided a clear and authoritative endorsement of litigation funding.⁷³ The case concerned an application to strike out for abuse of process on the basis that the litigation had been commercially funded by a third party. It was, therefore, an unusual vehicle for considering the principles of maintenance and champerty, the relief for which had never included a stay of proceedings. Indeed, *Trendtex* in England had concluded that the principles did *not* establish a defence or grounds for a stay.⁷⁴

The defendants' criticisms centred around three features of the arrangements: the recruitment of claimants by Firmstones (the funder), Firmstones' control of the litigation, and the profit that Firmstones would make. None of these constituted an abuse of the court's process.⁷⁵ In relation to the question of funder control, the plurality endorsed a particularly permissive approach, stating that:⁷⁶

many people seek profit from assisting the processes of litigation. That a person who hazards funds in litigation wishes to control the litigation is hardly surprising. That someone seeks out those who may have a claim and excites litigation where otherwise there would be none could be condemned as contrary to public policy only if a general rule against the maintenance of actions were to be adopted. But that approach has long since been abandoned...

This statement accommodates the commercial realities of funding arrangements: it is hardly rational for a person to fund litigation if they have no control

⁷³ *Jeffery & Katauskas Pty Ltd v SST Consulting Pty Ltd* [2009] HCA 43; (2009) 239 CLR 75, [29]-[30].

⁷⁴ *Fostif* (n 63) [79]-[82].

⁷⁵ *ibid* [88].

⁷⁶ *ibid* [89].

over it. Nevertheless, as will be seen, other common law jurisdictions are less sanguine about the prospect of funder control.

The plurality also referred to the possibility of concerns about the potential for funders to exploit vulnerably claimants, conflicts of duties arising for lawyers, fears about the effect on witnesses, and specific problems that might arise in group proceedings. But they concluded that a general public policy against funding would ‘take too broad an axe’ to any such difficulties, which could be resolved by specific measures (such as regulation in the class action context, or existing lawyers’ duties).⁷⁷

The continuing operation of the rule, and further exceptions

The doctrines of maintenance and champerty continue to prevent two practices:⁷⁸ the assignment of a bare cause of action,⁷⁹ and the use of contingency fee agreements by solicitors. Even here, though, the courts have continued to erode the doctrines,⁸⁰ and further exceptions have been created by statute.

Assignments

It remains the law that the assignment of a bare right to litigate will not be recognised,⁸¹ and that where the assignment is for the purpose of the assignor profiting, the assignment will be void as champertous.⁸²

⁷⁷ *ibid* [90]-[95].

⁷⁸ *Giles* (n 26)153.

⁷⁹ *Radin* (n 2) 67-8. See, eg, *Laurent v Sale & Co* [1963] 1 WLR 829 (HC); *Trendtex Trading Corporation v Credit Suisse* [1982] AC 679 (HL).

⁸⁰ *Trendtex* (n 79) 702-3; *Massai Aviation Services v Attorney General (The Bahamas)* [2007] UKPC 12, [16].

⁸¹ *Trendtex* (n 79); *Massai Aviation Services* (n 80) [15]; *Simpson v Norfolk & Norwich University Hospital NHS Trust* [2011] EWCA Civ 1149; [2012] QB 640, [15]; *JEB Recoveries LLP v Binstock* [2015] EWHC 1063 (Ch), [51];

⁸² *Simpson* (n 81).

The rule against assignments is limited. A debt is assignable because it is treated as a property right, even if it is disputed and litigation is required for enforcement,⁸³ although it has been recognised that this is a difficult distinction to draw.⁸⁴ Sales of debts are common and uncontroversial.⁸⁵ Assigning a debt to a special purpose vehicle in order to facilitate litigation is not champertous.⁸⁶ It is also not champertous to assign a restitutionary claim for money had and received under an unenforceable contract.⁸⁷ On the other hand, a claim for damages for repudiation of a contract,⁸⁸ or a tort claim,⁸⁹ cannot be assigned.

But there are four exceptions to the general rule. First, if a property right is assigned, then an associated right to litigate may be assigned with it.⁹⁰ Secondly, the fruits of a cause of action may be assigned (i.e. the potential proceeds of the claim).⁹¹ Thirdly, a bare cause of action may be assigned where the assignee had a genuine commercial interest in the claim.⁹² Fourthly, a statutory exception has long been recognised for insolvency practitioners and trustees in bankruptcy.

⁸³ *Camdex v Bank of Zambia* [1998] QB 22; *Botsman v Bolitho* [2018] VSCA 278, [25]; Greg Tolhurst, *The Assignment of Contractual Rights* (Hart 2006), [6.59].

⁸⁴ Andrew Cheng, 'Assignment of Bare Rights to Litigate: Assessing the Modern Doctrinal Position' (Honours thesis, University of Sydney 2014), 7-8.

⁸⁵ *Massai Aviation Services* (n 80) [18].

⁸⁶ *JEB Recoveries* (n 81) [53].

⁸⁷ *Equuscorp Pty Ltd v Haxton* [2012] HCA 7; (2012) 246 CLR 498, [53]; *Casehub Ltd v Wolf Cola Ltd* [2017] EWHC 1169 (Ch); [2017] 5 Costs LR 835, [25]-[26].

⁸⁸ *Ndole Assets Ltd v Designer M & E Services UK Ltd* [2017] EWHC 1148 (TCC); [2017] 1 WLR 4367, [62]-[63].

⁸⁹ Tolhurst (n 83) [6.59]; Anthony Guest and Ying Khai Liew, *Guest on the Law of Assignment* (2nd edn, Sweet & Maxwell 2015), [4-25].

⁹⁰ *Trendtex* (n 79) 70; citing *Ellis v Torrington* [1920] 1 KB 399 (CA).

⁹¹ *Glegg v Bromley* [1912] 3 KB 474 (CA), 484; Cheng (n 84) 8-9.

⁹² *Trendtex* (n 79) 703; *Massai Aviation Services* (n 80) [20]-[21]; *Equuscorp* (n 87) [53]; *Ndole Assets* (n 88) [64]. As to the difficulties in identifying what is a genuine commercial interest, see Cheng (n 84) 20-34.

The exceptional position of insolvency practitioners

As early as 1880, the Court of Appeal held that the *Bankruptcy Act 1869* enabled a trustee in bankruptcy to assign a cause of action which was the property of the bankrupt. Whilst this arose from the terms of the statute,⁹³ Jessel MR (with whom James LJ agreed) recognised that there were good policy reasons in support of that conclusion:⁹⁴

The proper office of the trustee is to realize the property for the sake of distributing the proceeds amongst the creditors. Why should we hold as a matter of policy that it is necessary for him to sue in his own name? He may have no funds, or he may be disinclined to run the risk of having to pay costs, or he may consider it undesirable to delay the winding-up of the bankruptcy till the end of the litigation.

In the following year, the Court of Appeal held that a liquidator, too, could dispose of a company's causes of action pursuant to the terms of the *Companies Act 1862*.⁹⁵ But a cause of action personal to a liquidator may not be assigned in England.⁹⁶

Similarly, in Australia, liquidators have the power to 'sell or otherwise dispose' of the property of a distressed company.⁹⁷ In 1996 and 1997, a series of judgments in various Australian courts confirmed that this power enabled liquidators to enter into litigation funding agreements.⁹⁸

⁹³ *Seear v Lawson* (1880) 15 Ch D 426 (CA), 433 (Jessel MR), 434 (James LJ and Brett LJ). See also 429-30 (Bacon V-C, at first instance).

⁹⁴ *ibid* 433 (Jessel MR).

⁹⁵ *In re Park Gate Waggon Works Company* (1881) 17 Ch D 234 (CA).

⁹⁶ *Re Ayala* [1996] 1 BCLC 467, 480-1, 483.

⁹⁷ Corporations Act 2001 (Cth), s 477(2)(c).

⁹⁸ *Re Movitor Pty Ltd* (1996) 64 FCR 380 (FCA); *UTSA Pty Ltd (in liq) v Ultra Tune Australia Pty Ltd* (1996) 21 ACSR 457 (CA(Vic)); *Re Tosich Construction Pty Ltd; Ex parte Wily* (1997) 23 ACSR 126 (FCA).

The position of solicitors

The broad definition of maintenance, taken literally, captures the ordinary professional role of the solicitor in litigation. This difficulty was avoided by treating the solicitor as having a legitimate interest in ‘intermeddling’ in litigation, provided they acted within the confines of their professional obligations.⁹⁹ But solicitors were prohibited from entering into champertous arrangements with their clients – that is, agreements to share the proceeds of litigation.¹⁰⁰ The reasons for the prohibition were twofold. First, it was perceived that the solicitor might impose ‘oppressive terms’ on the claimant, owing to their knowledge of their client’s circumstances.¹⁰¹ But the more important concern was for the opponent, who was said to have¹⁰²

... the right to be free from litigation conducted by the assistance of persons working for their own interests, and not in order to give lawful professional aid to the opposing litigant.

A lawyer who entered a champertous agreement with a client was treated harshly. They could not recover their fees, even on a quantum meruit basis,¹⁰³ a departure from the usual rule where a party has performed work pursuant to an illegal contract.¹⁰⁴ Further, even where an honest solicitor had mistakenly entered a champertous agreement, they could not be indemnified for any losses suffered thereby, as any policy for indemnity would also be void.¹⁰⁵

⁹⁹ *Wild v Simpson* [1919] 2 KB 544 (CA), 562.

¹⁰⁰ See, eg, *In re Trepca Mines* (n 26).

¹⁰¹ *Wild* (n 99) 563.

¹⁰² *ibid.*

¹⁰³ *ibid* 565-6 (Atkin LJ); *Awwad v Geraghty & Co (A Firm)* [2001] QB 570, 596.

¹⁰⁴ HG Beale, *Chitty on Contracts* (33rd edn, Sweet & Maxwell 2018), [16-225]-[16-226].

¹⁰⁵ *Haseldine v Hosken* [1933] 1 KB 822 (CA).

There was, however, a contradiction. The prohibition of maintenance and champerty was directed to protecting the interests of the *opponent* of the maintained party. But the consequence of a finding of champerty was merely that the solicitor was unable to seek his fees from his client, the maintained party; the proceedings would not be void.¹⁰⁶ Thus, a rule ostensibly intended to protect the interests of the opponent did not, in fact, alter the position of the opponent in the case at bar. An action for maintenance could be brought separately, but only in limited circumstances.¹⁰⁷

There was a further contradiction in the position of solicitors. There was no wrongdoing if a solicitor knowingly acted in champertously-funded litigation, provided that their own retainer was not champertous, and that they did not assist in the champertous agreement (for example by drafting it).¹⁰⁸ It is difficult to reconcile this with the suggestion that champerty sought to protect the interests of justice, and of the defendant.

The Australian High Court has adopted the English common law position that the ordinary conduct of litigation by a legal practitioner will not constitute maintenance, despite the fact that it would otherwise answer the broad definition of maintenance.¹⁰⁹ There are, however, two qualifications: the lawyer must consider that the client has a reasonable case, and must not engage in any champertous arrangement with the client.¹¹⁰

¹⁰⁶ *Wild* (n 99) 563 (Atkin LJ).

¹⁰⁷ An action for maintenance requires the claimant to prove special damage; it is not sufficient that the defendant's maintenance of an action has caused the claimant to incur legal expenses: *Neville v London 'Express' Newspaper Limited* [1919] AC 368 (HL), 480 (Lord Finlay LC); *Magic Menu Systems Pty Ltd v AFA Facilitation Pty Ltd* (1997) 72 FCR 261 (FCAFC), 269.

¹⁰⁸ *In re Trepcia Mines* (n 26) 220-1.

¹⁰⁹ *Clyne* (n 69) 203-5.

¹¹⁰ *ibid* 203.

In both jurisdictions, statute has modified the position. In England, solicitors may enter conditional fee agreements and damages-based agreements. But owing to the underlying prohibition, an agreement which does not comply with the legislation will be void for maintenance and champerty.¹¹¹ In all Australian jurisdictions, solicitors may now enter conditional costs agreements.¹¹²

Access to justice – a force for change

The principle of access to justice has driven judicial acceptance of litigation funding.¹¹³ Initially, courts recognised that the rules of maintenance and champerty – which initially prevented the oppression of litigants – had, themselves, a tendency to create oppression, by preventing the poor from seeking assistance to access the court.¹¹⁴ The 1990s saw the nascence of the litigation funding industry in Australia, and embryonic forms of funding in England. In sanctioning these new forms of funding, and in shrinking the operation of maintenance and champerty, courts were express about their intention to ‘recognise the need for innovative but responsible ways of increasing access to justice for the impecunious’.¹¹⁵ In England, the change of public policy was

¹¹¹ *Beach Petroleum NL v Abbott Tout Russell Kennedy* [1999] NSWCA 408; (1999) 48 NSWLR 1.

¹¹² Adrian Zuckerman and others, *Zuckerman on Australian Civil Procedure* (LexisNexis Butterworths 2018), [28.189]-[28.193].

¹¹³ *Martell* (n 35) 386-7; *Magic Menu Systems* (n 107) 267; *Elfic v Macks* [2001] QCA 219; [2003] 2 Qd R 125, [67]; *Factortame* (n 51) [62]; *Sibthorpe v Southwark London Borough Council* [2011] EWCA Civ 25; [2011] 1 WLR 2111, [49]; *Casehub* (n 87) [28(5)]; Vicki Waye, *Trading in Legal Claims: Law, Policy & Future Directions in Australia, UK & US* (Presidian Legal Publications 2008), 5-6.

¹¹⁴ *Norglen Ltd v Reeds Rains Prudential Ltd* [1999] 2 AC 1, 11; *Massai Aviation Services* (n 80) [13].

¹¹⁵ *Elfic* (n 113) [65].

described by the Court of Appeal in the following terms, which have been approved in Australia¹¹⁶

Public policy now recognises that it is desirable, in order to facilitate access to justice, that third parties should provide assistance designed to ensure that those who are involved in litigation have the benefit of legal representation.

Thus, litigation funding was perceived as one solution to the perennial problem of high costs preventing those of limited means from accessing the court. Courts recognised that:¹¹⁷

... impecunious litigants may only be able to obtain access to justice if they can, in effect, promise to pay lawyers or experts or others whose services they require out of the proceeds of the litigation.

Access to justice considerations have also driven the court's approach to regulating litigation funding agreements. Nowhere is this more evident than in the context of Australian class actions, where – as we will see in Chapter 9 – successive courts have crafted a regulatory regime that seeks to ensure certainty for funders. In doing so, judges have been driven by access to justice considerations: specifically, the recognition that the class action regime would be unworkable without third party funding. In England, the justification for the *Arkin* cap (which limited the funder's

¹¹⁶ *Gulf Azov Shipping Co Ltd v Chief Idisi* [2004] EWCA Civ 292, [54]. See also *Sibthorpe* (n 113) [49]. As to Australian cases, see, eg, *Magic Menu Systems* (n 107) 267E; *Elfic* (n 113) [65]; *Clairs Keeley (A Firm) v Treacy and Others* [2004] WASCA 277; (2004) 29 WAR 479, [125]; *Fostif* (n 63) [65]; *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148; (2016) 245 FCR 191, [183]. This is also true in other common law jurisdictions; for example, as to the position in Cayman, see *Quayum v Hexagon Trust Company (CI) Ltd* 2002 CILR 161 (Grand Court), [61].

¹¹⁷ *Mansell v Robinson* [2007] EWHC 101 (QB); [2007] All ER (D) 279, referring to the Court of Appeal's reasoning in *Hamilton v Al-Fayed (No 2)* [2002] EWCA Civ 665; [2003] QB 1175 and *Factortame* (n 51).

exposure to adverse costs) was the premise that the value of funding was in aiding impecunious claimants.¹¹⁸

Law reform commissions also recognised and endorsed these developments, concluding time and again that there is social value in permitting external funding to facilitate access to justice, and recognising that this has driven courts to alter their approach to maintenance and champerty.¹¹⁹

Indeed, some have regretted the fact that the acceptance of litigation funding has been considered necessary in order to promote access to justice. Keane J, writing extra-judicially, has argued that access to justice has been an ‘effective password allowing incursions upon the administration of justice which would, in the past, have been repulsed by the courts’,¹²⁰ including the practice of litigation funding. In a similar vein, Gleeson CJ (speaking extra-judicially) observed that¹²¹

Litigation funding is now with us. Entrepreneurial activity in this respect ... is not in all respects attractive, but subject to certain controls it may be a necessity. There is a need for some pragmatism about this, because the cost of access to justice is essentially a practical matter.

Thus, on this view, litigation funding remains undesirable for the policy reasons which grounded the doctrines of maintenance and champerty, but pragmatism, and the competing value of access to justice, require that it be tolerated.¹²²

¹¹⁸ *Arkin v Borchard Lines (Nos 2 and 3)* [2005] EWCA Civ 655; [2005] 1 WLR 3055, [38]. The *Arkin* cap is addressed in Chapter 9 of this thesis.

¹¹⁹ See, for example, New South Wales Law Reform Commission, *Barratry, Maintenance and Champerty (Discussion Paper 36)* (1994), [2.55]; Standing Committee of Attorneys-General (n 70), [1.2]; *Review of Civil Litigation Costs: Preliminary Report* (2009), Chapter 15, [1.1]. See also *Review of Civil Litigation Costs: Final Report* (2009), [1.2]; *Regulation of Third Party Funding in Australia: Position Paper* (2011), [43].

¹²⁰ P A Keane, ‘Access to Justice and other Shibboleths’ (JCA Colloquium, Melbourne, 10 October 2009), 1.

¹²¹ Chief Justice Murray Gleeson, ‘Some Legal Scenery’ (Judicial Conference of Australia, Sydney, 5 October 2007), 8-9.

¹²² On this point, see also *Sibthorpe* (n 113) [49].

Two critical points must be noted. First, the attenuation of maintenance and champerty, and the judicial sanction given to litigation funding, was largely driven by access to justice considerations. It was not driven by the view that maintenance and champerty were entirely obsolete, or that they were driven by policy considerations which were now entirely irrelevant. Thus, maintenance and champerty – and the supporting policy considerations – continue to form the outer bound of permissible funding agreements.

Secondly, the access to justice considerations which drove these changes were access to the court for the impecunious (and, in Australia, class action claimants). It is, therefore, difficult to justify litigation funding entirely using this conventional ‘access to justice’ argument. I will consider the implications of this in detail in Chapter 7.

Policy concerns still remain

Courts have made clear that maintenance and champerty must evolve with public policy,¹²³ and that the tendency is to decrease the scope of their operation.¹²⁴

Four central policy concerns remain. As we will see in later chapters, these concerns correspond to criticisms which are made of litigation funding. These are:

- The idea that litigation ought not to be stirred up where it would otherwise remain dormant. I suggest that it is implicit in this idea that litigation is in some way undesirable. This is addressed in Chapter 3.

¹²³ *Hill* (n 34) 697; *Giles* (n 26) 164; *Thai Trading* (n 50) 786; *Simpson* (n 81) [24]; *Casehub* (n 87) [17].

¹²⁴ *Trendtex Trading Corporation and Another v Credit Suisse* [1980] QB 629, 663; *Camdex* (n 83) 29; *Factortame* (n 51) [91]; *Sibthorpe* (n 113) [44].

- A concern about the prospect of a third party being involved in litigation. The suggestion is that the involvement of a third party involves a departure from the ‘usual’ or ‘correct’ way to conduct litigation. This is addressed in Chapter 4.
- A concern about the prospect of commodifying some aspect of the civil justice system. This is addressed in Chapter 5.
- A suggestion that there might be harmful consequences of maintenance and champerty – specifically, the abuse of the court’s process. This may easily be dismissed, and is addressed briefly at the conclusion of Chapter 3.

The current position

The highest courts in England and Australia have held that commercial litigation funding agreements are not void, *per se*, for maintenance and champerty. The litigation funding industry has blossomed in both jurisdictions, as will be described later in this thesis. What, then is the controversy?

First, courts in England and Australia were frequently driven by pragmatism – rather than principle – in giving judicial sanction to litigation funding. Specifically, it was accepted that the value of access to justice outweighed the policy concerns which motivated maintenance and champerty. In England in particular, it continues to be recognised that the public policy principles underpinning maintenance and champerty have continued application, and may still be used to invalidate particular funding arrangements. As I have demonstrated in this chapter, and will develop in later chapters, there continues to be judicial and extrajudicial disquiet or concern about the use of litigation funding in both jurisdictions.

Are these concerns still well-founded? Is pragmatism, and concern about access to justice, the only reason why litigation funding should be permitted?

Secondly, the place of litigation funding in the civil justice system is not settled.

Important outstanding questions include:

- Is there anything wrong with litigation funding stirring up litigation where it would otherwise not exist?
- Is it permissible for the funder to control litigation? To what extent?
- In what circumstances will funders be liable for adverse costs?
- To whom does a solicitor owe their ethical obligations when litigation is funded by a third party?
- Does the court have power to supervise or regulate the behaviour of funders?

These questions will be addressed in this thesis. As will be seen, the approach of the court to these questions has often been haphazard and unsatisfactory.

Conclusion

The historical constraints on litigation funding were the doctrines of maintenance and champerty. This chapter has explained that these doctrines arose in the context of a mediaeval civil justice system which is unrecognisable to modern eyes. It has been recognised that public policy has changed, and the doctrines are much diminished – although they still form the outer bounds of permissible funding agreements.

Today, the public policy basis for maintenance and champerty is the need to protect the integrity of the judicial process and the interests of defendants. As will be seen, vestiges of the policy concerns remain. The following three chapters address those concerns.

CHAPTER 3 – IS LITIGATION DESIRABLE?

Introduction

In Chapter 2, I identified that there were four policy concerns which underpinned the modern doctrine of maintenance and champerty (and the remaining concerns about litigation funding). This chapter addresses the first: the idea that litigation ought not to be stirred up where it would otherwise remain dormant (which I suggest implies a view that litigation is, in some way, undesirable).

What is the objection?

One thing that opponents and proponents of litigation investment generally agree on is that it is likely to have the effect that lawsuits will be able to be brought where otherwise they could not have been. Accordingly, it has a tendency to increase litigation.¹ It is apparent that some of the objections about litigation funding are really objections to litigation: the desirability of any external funding for litigation is contingent on ‘the underlying social value of litigation’.²

Maintenance and champerty have long reflected the sentiment that litigation ought to be dreaded ‘beyond almost anything else short of sickness and death’,³ and

¹ However, it should be noted that there are some who suggest that the availability of litigation funding will ultimately have a deterrent effect on potential wrongdoers, thus leading to a decrease in the quantity of litigation. David Dana and Max Schanzenbach, ‘How Would Third Party Financing Change the Face of American Tort Litigation? The Role of Agency Costs in the Attorney-Client Relationship’ (Public Policy Roundtable on Third Party Financing of Litigation, Northwestern Law School, 24-25 September 2009), 2, 9; Steven Garber, *Occasional Paper - Alternative Litigation Financing in the United States: Issues, Knowns and Unknowns* (2010), 29; Charles Silver, ‘Litigation Funding versus Liability Insurance: What’s the Difference?’ (2014) 63 DePaul Law Review 617, 650-1.

² Samuel Issacharoff, ‘Litigation Funding and the Problem of Agency Cost in Representative Actions’ (2014) 63 DePaul Law Review 561, 566.

³ Judge Learned Hand, ‘The Deficiencies of Trials to Reach the Heart of the Matter’ in James Rosenberg and others (eds), *Lectures on Legal Topics 1921-1922* (Macmillan 1926), 105, cited

that the vice of the practices were, in part, ‘stirring up litigation and strife’.⁴ In the first half of the 19th century, Lord Abinger CB expressed this sentiment in the following terms:⁵

All our cases of maintenance and champerty are founded on the principle that no encouragement should be given to litigation by the introduction of parties to enforce those rights which others are not disposed to enforce.

Thus, it was critical that the claimant make the decision whether or not to litigate. This was sometimes expressed in terms of a defendant’s right not to be troubled by litigation where it was aided by third parties.⁶

Courts in England⁷ and Australia⁸ have recognised that a desire not to encourage litigation motivated the prohibition of maintenance. Some judges have acknowledged that this is an outdated view;⁹ but this perspective is by no means universal. For example, in *Fostif*, the minority expressed the view that:¹⁰

Court process is ... coercive and otherwise injurious both to litigants and to third parties and should not be employed beyond legitimate necessity.

Criticism of litigation funding continues to include the suggestion that litigation is, itself, undesirable. It is unsurprising to find that some of the most vociferous

by Callinan and Heydon JJ at *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* [2006] HCA 41; (2006) 229 CLR 386 [274]. See also, for example, Chief Justice Murray Gleeson, ‘The Purpose of Litigation’ (The Martin Kriewaldt Memorial Address, Darwin, 12 August 2008), 21.

⁴ *Findon v Parker* (1843) 11 M & W 675; 152 ER 976, 680. See also *Ram Coomar Coondoo v Chunder Canto Mookerjee* (1876) 2 App Cas 186 (PC), 207-8.

⁵ *Prosser v Edmonds* 1 Y & C 481, 203, 497. See also *Alabaster v Harness* [1895] 1 QB 339 (CA), 344 (Lopes LJ).

⁶ *Neville v London 'Express' Newspaper Limited* [1919] AC 368 (HL), 395; *Wild v Simpson* [1919] 2 KB 544 (CA), 563.

⁷ *In re Trepca Mines Ltd (No 2)* [1963] 1 Ch 199 (CA), 219.

⁸ *Magic Menu Systems Pty Ltd v AFA Facilitation Pty Ltd* (1997) 72 FCR 261 (FCAFC), 267.

⁹ *Thai Trading Co v Taylor* [1998] QB 781 (CA).

¹⁰ *Fostif* (n 3) [266] (citations omitted, emphasis added).

opposition to litigation investment comes from business lobby groups.¹¹ Cameron and Kalajdzic, for example, observe that the views expressed by chambers of commerce about the merits of litigation funding often mirror the views expressed as to the merit of litigation as a means of commercial dispute resolution.¹²

Recent developments in Australian class actions have provided a particularly stark example of hostility to litigation funding being spurred on by hostility to litigation. Longstanding controversies about the use of funding in Australian class actions will be addressed in later chapters,¹³ but for present purposes it is sufficient to note that a particular area of controversy has been funded securities class actions for breaches of continuous disclosure obligations. In short, it has been suggested that the Australian law on continuous disclosure has undesirable economic effects, which are exacerbated by the use of class actions.¹⁴ There were fears that the COVID-19 pandemic might lead to more claims in this area. On 22 May 2020, the Treasurer used emergency powers, granted to deal with the pandemic, to announce that litigation funders would be required to hold an Australian Financial Services Licence (imposing onerous regulatory obligations), despite the opposition of the corporate regulator, and in the face of contrary recommendations made by the Australian Law Reform Commission in its

¹¹ See, for example, US Chamber Institute for Legal Reform, ‘Selling Lawsuits, Buying Trouble: Third-Party Litigation Funding in the United States’ (2009) <<http://www.instituteforlegalreform.com/uploads/sites/1/thirdpartylitigationfinancing.pdf>> accessed 19 May 2015; US Chamber Institute for Legal Reform, ‘Stopping the Sale on Lawsuits: A Proposal to Regulate Third-Party Investments in Litigation’ (2012) <http://www.instituteforlegalreform.com/uploads/sites/1/TPLF_Solutions.pdf> accessed 19 May 2015.

¹² Camille Cameron and Jasminka Kalajdzic, ‘Commercial Litigation Funding: Ethical, Regulatory and Comparative Perspectives’ (2014) 55 *Canadian Business Law Journal* 1, 4.

¹³ Principally in Chapters 9, 10 and 11.

¹⁴ See generally the discussion by the Australian Law Reform Commission, *Integrity, Fairness and Efficiency—An Inquiry into Class Action Proceedings and Third-Party Litigation Funders (ALRC Report 134)* (2018), Chapter 9.

most recent treatment of litigation funding.¹⁵ The changes occurred in the context of long-standing pressure from business lobby groups, and it was reported that, in explaining the changes, ‘Mr Frydenberg [the Treasurer] said Australian companies needed to stay in business in the current crisis rather than spend time “fending off” class actions.’¹⁶

In the academic literature, one view is that litigation is undesirable because of its economic consequences.¹⁷ The argument, in effect, is that litigation is undesirable because it diverts the resources of the defendants away from more economically rewarding activities, and creates a disincentive to entrepreneurial behaviour.¹⁸ It might also be said that the question is one of degree: Jolowicz has argued that if there is insufficient disincentive to litigate (in the form of cost or delay, for example), the volume of litigation will increase to a point where the courts will be over-burdened, because civil justice is ‘inherently expensive and time-consuming’.¹⁹

¹⁵ Ben Butler, ‘Frydenberg’s Changes to Shareholder Class Actions Smack of ‘Cronyism’, Lawyers Say’ *The Guardian* (25 May 2020) <<https://www.theguardian.com/australia-news/2020/may/25/frydenbergs-changes-to-shareholder-class-actions-smack-of-cronyism-lawyers-say>> ; see also The Hon Josh Frydenberg MP, *Litigation funders to be regulated under the Corporations Act* (2020).

¹⁶ David Crowe, ‘New rules for litigation funders after jump in class actions’ *Sydney Morning Herald* (22 May 2020) <<https://www.smh.com.au/politics/federal/new-rules-for-litigation-funders-after-jump-in-class-actions-20200521-p54vak.html>> .

¹⁷ See, eg, Jeremy Kidd, ‘To Fund or not to Fund: The Need for Second-Best Solutions to the Litigation Finance Dilemma’ (2012) 8 *Journal of Law, Economics and Policy* 613, 622-4, who clearly identifies the economic costs of litigation, before turning to the question whether any increase because of funding costs is justified – in particular, whether any additional claims are more likely to be frivolous. See also the material cited by Geoffrey J Lysaught and D Scott Hazelgrove, ‘Economic Implications of Third-Party Litigation Financing on the U.S. Civil Justice System’ (2012) 8 *Journal of Law, Economics and Policy* 645, footnotes 31-33. It may be that this arises in the United States because there are fewer impediments to plaintiffs to litigate: see, eg, Lysaught, 645, 653.

¹⁸ Lysaught (n 17) 653-4.

¹⁹ JA Jolowicz, *On Civil Procedure* (Cambridge University Press 2000), 71-3.

The ‘radiating effects’ of courts

Whilst litigation might be difficult, distracting and expensive for the individual litigant – such that it ought to be avoided – the process of litigation has broader social benefits. The suggestion that litigation is undesirable may be rebutted by identifying those benefits.

Courts do not advance dispute resolution simply by adjudicating on particular cases. In a common law system, the process of litigation serves, broadly, two additional purposes. First, court proceedings identify and develop the content of the substantive law. Secondly, they also demonstrate, in a broader sense, ‘the effectiveness of the law’;²⁰ litigation demonstrates to non-litigants that, in the event that they or their counterparties fails to fulfil their obligations under the substantive law, there is recourse to a court.²¹ Thus,²²

The principal contribution of courts to dispute resolution is the provision of a background of norms and procedures, against which negotiations and regulation... takes place. ... Courts communicate not only the rules that would govern adjudication of the dispute, but also possible remedies and estimates of the difficulty, certainty, and costs of securing particular outcomes.

It is self-evident that in order for courts to provide this ‘background of norms and procedures’, there must be cases brought before court: ‘a flow of adjudicated cases is necessary to provide guidance on the law and, most importantly, to create the credible

²⁰ *ibid* 71. See also JA Jolowicz, ‘On the Nature and Purposes of Civil Procedural Law’ in IR Scott (ed), *International Perspectives on Civil Justice: Essays in Honour of Sir Jack IH Jacob QC* (Sweet & Maxwell 1990), 37.

²¹ Jolowicz, ‘On the Nature and Purposes of Civil Procedural Law’ (n 20) 36-7; Jolowicz *On Civil Procedure* (n 19) 70-1; Alexandra Lahav, *In Praise of Litigation* (Oxford University Press 2017), 87.

²² Marc Galanter, ‘The Radiating Effects of Courts’ in Keith O Boyum and Lynn M Mather (eds), *Empirical Theories about Courts* (Longman 1983), 121. See also Richard O Lempert, ‘More Tales of Two Courts: Exploring Changes in the Dispute Settlement Function of Trial Courts’ (1978) 13 *Law & Society Review* 91, 99-100 as to the various ways courts aid dispute resolution beyond adjudication.

threat of litigation if settlement is not achieved'.²³ Clearly, this requires a critical mass of litigation to be brought.

But it is not just the volume of cases which is important. Cases before the court, and the opportunities to develop the law, reflect what is commenced – which is partly determined by access to legal resources.²⁴ There are good reasons for wanting the cases which are brought before the court to be representative of the disputes which arise in the community. As Kidd explains:²⁵

On a very basic level, it is disquieting to think that certain socioeconomic classes in our society may find themselves effectively barred from the remedial institutions designed to protect all citizens, regardless of means. From an economic standpoint, the prospects are equally disturbing, for the inability of lower socioeconomic classes to obtain compensation for tortious harms means that tort law will provide woefully incomplete deterrence to behavior which burdens not only the victim, but also society's economic productivity. Moreover, if tort law provides deterrence unequally between socioeconomic classes, there will be distortionary effects.

It is obvious that if law is not enforced by courts – if torts and breaches of contract go unremedied – then there is injustice to individuals, and the deterrent effect of law is diminished. But there is also a more subtle, but more pernicious effect: it diminishes the legitimacy of the law, and of the institutions which make and enforce law. This, in turn, has a tendency to diminish compliance.

This point may be explained by starting with the observation that legal rules are only effective and authoritative if there is a threshold level of compliance;²⁶ a lawmaker 'must be able to anticipate that the citizenry as a whole will accept as law and generally

²³ Hazel Genn, *Judging Civil Justice* (Cambridge University Press 2010), 21.

²⁴ *ibid.*

²⁵ Kidd (n 17) 620.

²⁶ Tom Tyler, *Why People Obey the Law* (rev edn, Princeton University Press 2006), 19.

observe the body of rules he has promulgated'.²⁷ Further, it is trite to observe that most of the time, people comply with the law not because of brute force, nor because of a court order requiring compliance. Indeed, even deterrence – the fear of adverse consequences arising from a breach of the law – may not create the necessary motivation to comply with the law.²⁸ Rather, people comply with the law if (and because) they regard the institution as legitimate.²⁹

There is evidence that the most important aspect of legitimacy is whether the institution observes procedural fairness: 'Views about authority are strongly connected to judgments of the fairness of the procedures through which authorities make decisions'.³⁰ Assessments of the procedural fairness of institutions are influenced by whether those involved 'hav[e] an opportunity to present their arguments, [are] listened to, and [have] their views considered by authorities', whether the decision-making process of the institution is unbiased, and whether the institution's procedures lead to fair results.³¹ These observations from empirical research conducted by social scientists are familiar; they are also the criteria by which courts measure their own procedural fairness.³² The importance of procedural fairness of an institution is well-explained in the following terms³³

Why might experiencing unfair procedures undermine the role of legitimacy in maintaining compliance? The obligation to obey is based on trust of authorities. Only if people can trust authorities, rules, and institutions can they believe that their own long-term interests are served

²⁷ Lon Fuller, 'Human Interaction and the Law' in Robert Paul Wolff (ed), *The Rule of Law* (Simon and Schuster 1971), 201.

²⁸ Tyler (n 26) 161, 165, 269-70, 275, 277.

²⁹ *ibid* 170.

³⁰ *ibid* 162, 273-4.

³¹ *ibid* 163-4.

³² Adrian Zuckerman, *Zuckerman on Civil Procedure: Principles of Practice* (3rd edn, Thomson Reuters, Sweet & Maxwell 2013) Chapter 3.

³³ Tyler (n 26) 172.

by loyalty towards the organization. In other words, the social contract is based on expectations about how authorities will act. If authorities violate these expectations, the social contract is disrupted. ... people appear to connect the obligations of authorities to issues of fair procedure, not to outcomes. It is being unfairly treated that disrupts the relationship of legitimacy to compliance, not receiving poor outcomes.

The point may be summarised as follows. If courts function with procedural fairness (which includes, I suggest, the idea that redress is not precluded because of a lack of means), then the legitimacy of the court is enhanced. This, in turn, enhances the likelihood of compliance with the law, because people are more likely to comply with the demands of institutions which are regarded as legitimate (and procedural fairness is critical to perceptions of legitimacy).

The suggestion that litigation is undesirable per se is therefore problematic. The legal system is necessary for peaceful social coexistence.³⁴ It offers the benefits of preventing and correcting injustices, and improving welfare – for example, through solving coordination problems and creating institutions such as private property and contract.³⁵ Access to the courts is critical for these benefits.³⁶

The rule of law

At a more fundamental level, adjudication, and the ability of all to access the court, are necessary for the maintenance of the rule of law. At its foundation, the rule of law has

³⁴ Thomas Hobbes and JCA Gaskin, *Leviathan* (Oxford University Press 1998), Chapter XIII.

³⁵ Frederick Wilmot-Smith, *Equal Justice: Fair Legal Systems in an Unfair World* (Harvard University Press 2019), 15-22.

³⁶ William Blackstone and others, *Commentaries on the Laws of England* (Oxford University Press 2016), [138].

two components: '(1) that people should be ruled by the law and obey it, and (2) that the law should be such that people will be able to be guided by it.'³⁷

From this base, more specific principles can be derived. One of these is the requirement of congruence:³⁸ that the law as it is stated must comport with the law as it is applied. In the absence of congruence, the law is a dead letter. Fuller regarded this as the 'most complex' aspect of the rule of law. He observed that it could be³⁹

destroyed or impaired in a great variety of ways: mistaken interpretation, **inaccessibility of the law**, lack of insight into what is required to maintain the integrity of a legal system, bribery, prejudice, indifference, stupidity, and the drive towards personal power. [emphasis added]

The first requirement is that of accessible courts. A further requirement is for independent judges. But judges are assisted and influenced by the lawyers who appear before them, which means that it is necessary for there to be some equality of arms between litigants.⁴⁰

Inequality of access to the court obviously has implications for the putative litigants. It also has systemic consequences: there are fewer opportunities to develop the law.

The judiciary is responsible for congruence.⁴¹ Fuller considered, though, that the risk of relying on courts for ensuring congruence between declared law and official

³⁷ Joseph Raz, *The Authority of Law: Essays on Law and Morality* (Clarendon Press 1979), 213; these are common themes: Brian Z Tamanaha, *On the Rule of Law: History, Politics, Theory* (Cambridge University Press 2004), chapter 9.

³⁸ Lon L Fuller, *The Morality of Law* (rev edn, Yale University Press 1969), 81; see generally 81-90; Wilmot-Smith (n 35) 80.

³⁹ Fuller (n 38) 81.

⁴⁰ Wilmot-Smith (n 35) 83, 85; Lahav (n 21) 117-18.

⁴¹ Fuller (n 38) 81.

action was that it ‘ma[de] the correction of abuses dependent on the willingness and financial ability of the affected party to take his case to litigation’.⁴²

Accessibility to the court as an aspect of the rule of law was explained in greater detail by Raz, who developed further the notion that rules cannot merely be declared – they must be *applied* consistently and correctly. This places great importance on the role of the court.⁴³ Having established the importance of courts applying rules correctly and fairly, the necessity of ensuring access to the courts followed:⁴⁴

The courts should be easily accessible. Given the central position of the courts in ensuring the rule of law... it is obvious that their accessibility is of paramount importance. Long delays, excessive costs, etc., may effectively turn the most enlightened law to a dead letter and frustrate one’s ability effectively to guide oneself by the law.

Like Raz, Finnis has emphasised that the requirements of the rule of law ‘involve qualities of institutions and processes’.⁴⁵ Amongst Finnis’ desiderata was the requirement that officials ‘do actually administer the law consistently and in accordance with its tenor’.⁴⁶ Further, promulgation requires more than mere publication of laws; it also requires that lawyers be available at reasonable cost ‘to advise anybody who wants to know where he stands’.⁴⁷ Finnis concluded:

At each point we see that the Rule of Law involves certain qualities of process which can be systematically secured only by the institution of judicial authority and its exercise by persons professionally equipped and motivated to act according to law. Obviously, much more could be said about this institutional aspect of the Rule of Law – of what **historical experience has shown to be further desiderata**, such as the independence of the judiciary, the openness of court proceedings, the power of the courts to review the

⁴² *ibid.*

⁴³ Raz (n 37) 216-17 (principles 4-6).

⁴⁴ *ibid* 217.

⁴⁵ John Finnis, *Natural Law and Natural Rights* (Oxford University Press 1980), 271.

⁴⁶ *ibid.* This is equivalent to Fuller’s requirement of congruence.

⁴⁷ *ibid.*

proceedings and actions not only of other courts but of most other classes of official, **and the accessibility of the courts to all, including the poor.** [emphasis added]

Thus, Finnis identifies – in his ‘institutional’ requirements of the rule of law – many of the same matters as Raz: judicial independence, judicial review of official action and – crucially – the accessibility of the court.

Bingham favoured a substantive version of the rule of law.⁴⁸ Nevertheless, his version of the eight desiderata of the rule of law includes the formal requirements, including the principle that ‘Means must be provided for resolving, without prohibitive cost or inordinate delay, bona fide civil disputes which the parties themselves are unable to resolve’.⁴⁹ Bingham expressed essentially the same point as Raz when he wrote that⁵⁰

It would seem to be an obvious implication of the principle that everyone is bound by and entitled to the protection of the law that people should be able, in the last resort, to go to court to have their civil rights and claims determined. **An unenforceable right or claim is a thing of little value to anyone.** [emphasis added]

The value of the rule of law

The rule of law is necessary for law to be effective in guiding conduct. It therefore has an *instrumental* value in securing whatever ends the substantive law seeks to achieve. More specifically, it has been said that the rule of law promotes an efficient market by

⁴⁸ Tom Bingham, *The Rule of Law* (Penguin 2011), 67; this includes, for example, ‘adequate protection of human rights’ – see chapter 7.

⁴⁹ *ibid* 85.

⁵⁰ *ibid* (emphasis added).

promoting stability and predictability in transactions,⁵¹ and there is evidence that compliance with the rule of law improves the economic development of a state.⁵²

However, irrespective of the content of the law, there is also an *intrinsic* value to the rule of law: it enables people to plan their lives by providing a reliable basis for them to predict the legal consequences of their conduct, and the conduct of others. It therefore treats people subject to the law as moral agents capable of self-direction, and thereby acknowledges their dignity.⁵³

Fuller describes this as the ‘inner morality’ of the rule of law.⁵⁴ Raz, despite disputing the link between law and morality, also argues that ‘observance of the rule of law is necessary if the law is to respect human dignity’.⁵⁵ This link between the rule of law and dignity is also made by Finnis, who identifies that ‘The fundamental point of the desiderata is to secure to the subjects of authority the dignity of self-direction and freedom from certain forms of manipulation’.⁵⁶ Both Raz and Finnis expressly identify that this virtue arises from the fact that compliance with the rule of law means that

⁵¹ *ibid* 38-9; Tamanaha (n 37) 119, 139-40.

⁵² Robert J Barro, *Determinants of Economic Growth: A Cross-Country Empirical Study* (MIT Press 1997), 26-9. See generally World Bank, ‘World Development Report 2017: Governance and the Law’ (2017) <<https://www.worldbank.org/en/publication/wdr2017>> accessed 30 July 2020. See also Lord David Neuberger, ‘From Barretty, Maintenance and Champerty to Litigation Funding’ (Harbour Litigation Funding First Annual Lecture, Gray's Inn, 8 May 2013), especially [9], [47], which draws heavily on Daron Acemoglu and James A Robinson, *Why Nations Fail: The Origins of Power, Prosperity and Poverty* (Profile Books 2012).

⁵³ See, eg, Fuller (n 38) 162.

⁵⁴ *ibid* 41, 162.

⁵⁵ Raz (n 37) 221, see generally 220-2.

⁵⁶ Finnis (n 45) 272-3. Unlike Raz, Finnis uses this to argue for a link between law and morality: in essence, Finnis contends that the rule of law indicates that the rule-maker has some respect for individuals, and that there is some reciprocity between the governor and the governed, in that one creates rules which can direct conduct, and the other uses those rules to guide their conduct: see 273-4.

people can plan their lives. In other words, the rule of law creates predictability, which furthers dignity by allowing people to shape their own lives.⁵⁷

Hayek (and other liberal scholars) regard the rule of law as crucial to liberty; this, rather than dignity, is treated as the value underpinning the rule of law.⁵⁸ But the promotion of liberty is said to arise because the rule of law enables people to plan their affairs and act with autonomy.⁵⁹ The ‘good’ that the rule of law promotes is therefore substantially the same, whether this is described in terms of dignity or liberty.⁶⁰

How does the inability to access the court harm the rule of law?

We have seen that leading accounts of the rule of law include the requirement of access to the court as an aspect of one or other of the desiderata. More specifically, the inability to access the court harms the rule of law in several ways.

First, if a wronged party cannot or will not obtain a court order in their favour, then the law provides no reason for the wrongdoer to comply with the law.⁶¹ A gap will therefore emerge between the law – the declared rules – and actual practice.

Secondly, a person who is restricted in their ability to access the court has no reason to expect others to fulfil their legal obligations towards them. Such a person

⁵⁷ *ibid* 272, see also 273.

⁵⁸ Tamanaha (n 37) 32, 65-6.

⁵⁹ *ibid* 94; Jeremy Waldron, ‘The Rule of Law in Contemporary Liberal Theory’ (1989) 2 *Ratio Juris* 79, 84-5.

⁶⁰ Contra Jeremy Waldron, ‘Is the Rule of Law an Essentially Contested Concept (in Florida)?’ (2002) 21 *Law and Philosophy* 137, 158, who says that the dispute about the value of the rule of law – whether it serves the purpose of dignity, freedom, or is instrumental to other goods – is one of the matters which leads to its being an essentially contested concept.

⁶¹ There may, of course, be non-legal reasons to comply with the law, such as a fear of social sanctions, or the need to transact again with the wronged party or others in the market.

will lose the benefit of the rule of law: the ability to plan for themselves by reference to the fixed and stable reference point that law provides.

Thirdly, these matters will diminish the law's ability to guide conduct. If the enforcement of law by a court is contingent on the claimant's appetite for litigation, then law loses its efficacy in guiding the conduct of those who deal with the claimant.

Finally, an inaccessible court diminishes the extent to which the law applies equally to all.⁶² It is obvious that precluding access to court on the legally irrelevant basis of a party's appetite for litigation will tend to produce the result that the application of the law will be unequal.

The rule of law and litigation funding

The solution to these problems is to ensure that access to court is not contingent on a claimant's appetite for, or ability to afford, the high and unpredictable costs of litigation.

Litigation funding is a solution, provided by the market. Clearly, it is not a perfect solution. For example, a rational commercial funder will only fund cases where the defendant has sufficient means to pay the claimant's costs and the judgment sum sought. But litigation funding improves compliance with the rule of law, specifically the criterion of accessibility of the court.

⁶² See, eg, David Luban, *Lawyers and Justice: An Ethical Study* (Princeton University Press 1988), 264; Ross Cranston, *How Law Works: The Machinery and Impact of Civil Justice* (Oxford University Press 2006), 41.

Alternative Dispute Resolution

For the reasons explained above, hostility to litigation is difficult to defend. But beyond the litigation funding context, it is also observed in the context of promoting alternative dispute resolution (ADR).

The modern civil justice system shows an inconsistent approach to the value of litigation. On one hand, the creation of rights, and the movement to make courts more accessible (for example, through the online court), indicate a recognition of the value of the court and the imperative to ensure that it is accessible to all. There is also an increasing trend towards ‘juristocracy’, the phenomenon in which issues are resolved by courts rather than other arms of government.⁶³ Access to justice initiatives of the sort discussed in Chapter 7, are premised on the desirability of litigation. On the other hand, alternative dispute resolution has a tendency to move people out of court, and where it is imposed on parties against their will it has a tendency to inhibit litigation which might otherwise have proceeded to adjudication.⁶⁴ So, too, do rules of court which incentivise settlement. It would be irrational for parties to continue litigation if an acceptable compromise were possible, but some rules of court serve to distort the financial incentives in a manner which tips the balance strongly against adjudication.⁶⁵ To this category might also be added the imposition of court fees set at a rate which

⁶³ Genn (n 23) 148.

⁶⁴ See the classic discussion of this (and settlement more broadly) in Owen Fiss, ‘Against Settlement’ (1984) 93 Yale Law Journal 1073.

⁶⁵ For example, the consequences of a party failing to beat an opponent’s CPR 36 offer are potentially punitive: see Zuckerman (n 32) [26.71]-[26.80]; as to the equivalent Australian provisions, see Adrian Zuckerman and others, *Zuckerman on Australian Civil Procedure* (LexisNexis Butterworths 2018), [27.93]-[27.112].

generates revenue.⁶⁶ These developments undermine the sense of there being social value in litigation and, in particular, in adjudication.

As explained earlier in this chapter, this thesis adopts the view that litigation is desirable and socially beneficial. But criticism of litigation funding on the basis that it increases litigation must be understood in a broader context of challenges to the social value of litigation,⁶⁷ and the existence of various policies which discourage litigation and undermine its social value.

Might litigation funding increase quantity but decrease quality?

An increase in litigation caused by litigation funding would be objectionable if the additional cases were disproportionately likely to involve some abuse of the court's process, or to be frivolous or unmeritorious.⁶⁸ Indeed, each of those concerns is expressed, but may be quickly dismissed.

Abuse of court process

One of the reasons for the prohibition of champerty was the fear of abuse of process.⁶⁹ When the doctrine emerged in mediaeval England, this fear was well-founded.⁷⁰

⁶⁶ Andrew Higgins, 'The Costs of Civil Justice and Who Pays?' (2017) 37 *Oxford Journal of Legal Studies*, 698-702.

⁶⁷ See, eg, *The Amptill Peerage* [1977] AC 547, 575E (Lord Simon); *Village/Nine Network v Mercantile Mutual* [1999] QCA 276, [27].

⁶⁸ In the sense of having a remote chance of success, and having been commenced only for the purpose of seeking to achieve an 'in terrorem' settlement or some other collateral purpose (rather than, for example, to drive change in the law).

⁶⁹ *Stanley, Administratrix of Thomas Stanley v Jones* (1831) 7 Bingham 369; 131 ER 143, 146-7; *Guy v Churchill* (1888) 40 Ch D 481, 488; *Giles v Thompson* [1994] 1 AC 142 (HL), 153; AH Dennis, 'The Law of Maintenance and Champerty' (1890) 6 *Law Quarterly Review* 169, 170-1, 3.

⁷⁰ See Chapter 2.

Despite the vast changes in court process since then, this view continues to have modern adherents.⁷¹ In a frequently-cited passage, Lord Denning MR explained that:⁷²

The reason why the common law condemns champerty is because of the abuses to which it may give rise. The common law fears that the champertous maintainer might be tempted, for his own personal gain, to inflame the damages, to suppress evidence, or even to suborn witnesses.

It is difficult to understand why a funder would be disproportionately likely to abuse the court's process. More specifically, it is difficult to understand why a funder would be more likely to abuse the court's process than a party, or a solicitor,⁷³ or an insurer, who may also have incentive to 'suppress evidence' for their own personal gain – and would be better-placed⁷⁴ than a funder to do so.

It is said that solicitors owe fiduciary duties to clients and ethical duties to the court, and can 'readily be controlled' by the court or a professional association, such that sanctions for contempt and abuses of the court's process may be deployed more quickly and easily.⁷⁵ But abuse of process is wrongful irrespective of the identity of the wrongdoer. If it is thought that imposing on funders (and other third parties) duties to the court would alleviate the risk of their abusing the court's process, then that seems to be a more obvious response, rather than adherence to the doctrines of maintenance

⁷¹ See, eg, *Factortame Ltd v Secretary of State for Transport, Local Government and the Regions (No 8)* [2002] EWCA Civ 932; [2003] QB 381, [36], [84]-[85]; *Clairs Keeley (A Firm) v Treacy and Others* [2004] WASCA 277; (2004) 29 WAR 479, [125], [132]; *Deloitte Touche Tohmatsu v JP Morgan Portfolio Services Ltd* [2007] FCAFC 52; (2007) 158 FCR 417, [39]; *Murphy & Ors v Gladstone Ports Corporation Ltd (No 4)* [2019] QSC 228, [144].

⁷² *In re Trepca Mines* (n 7) 219-20. See also *Deloitte Touche Tohmatsu* (n 71), [39].

⁷³ See, for example, *Thai Trading* (n 9) 790 as to the incentives for a solicitor to engage in abuse of the court's process.

⁷⁴ An insurer would be better-placed owing to the usual insurance practice of taking over conduct of litigation: this is discussed in Chapter 11.

⁷⁵ *Fostif* (n 3) 487.

and champerty – indeed, some Australian jurisdictions have rules of court which do precisely that.⁷⁶

Whilst any litigation theoretically involves a risk of abuse of process by a participant, the court has a wide jurisdiction to guard against abuses. Indeed, in Australia, the doctrine of abuse of process has been used to curtail the use of class actions in some circumstances: it is an abuse of process to commence proceedings for the purpose of generating fees for the solicitor,⁷⁷ or in the hope of obtaining a court order for compensation for time and effort spent as lead plaintiff or for funding the litigation (qua lead plaintiff).⁷⁸ The doctrine of abuse of process has also been used to restrain a solicitor and counsel from acting for a class in circumstances where they had a financial interest in the litigation funder.⁷⁹

Concerns about abuse of process may therefore be quickly dismissed. They are a vestige of concerns about the conduct of mediaeval litigation which are entirely misplaced in the modern civil justice system.

An increase in frivolous litigation?

A separate claim is made that third party funding is disproportionately likely to encourage frivolous or unmeritorious litigation.⁸⁰ In the US literature, this assertion is

⁷⁶ Discussed in Chapter 9.

⁷⁷ *Treasury Wine Estates Ltd v Melbourne City Investments Pty Ltd* [2014] VSCA 351; (2014) 45 VR 585, [11]-[14]. The solicitor, Mark Elliott, was also the sole director and shareholder of the lead claimant, MCI. MCI had been incorporated as a vehicle for bringing class actions for breaches of continuous disclosure obligations. It held only a small parcel of shares, so its recovery from the class action could only be very small. The judgment was followed in *Melbourne City Investments Pty Ltd v Leighton Holdings Limited* [2015] VSCA 235, [45].

⁷⁸ *Melbourne City Investments Pty Ltd v Myer Holdings Ltd* [2017] VSCA 187; (2017) 53 VR 709, [32] and [46]-[50].

⁷⁹ *Bolitho v Banksia Securities Limited (No 4)* [2014] VSC 582, discussed in Chapter 11.

⁸⁰ See, eg Paul H Rubin, 'Third-Party Financing of Litigation' (2011) 38 Northern Kentucky Law Review 673; Kidd (n 17); Michael Abramowicz, 'Litigation Finance and the Problem of Frivolous Litigation' (2014) 63 DePaul Law Review 195, 196-7.

often based on the premise that meritorious litigation is likely to be funded by contingency fees, such that litigation investment will fund only litigation which was insufficiently prospective for the contingency fee lawyer,⁸¹ or arises in the context of consumer litigation funding. Consumer litigation lending operates on a business model which works on volume and entails little screening. It is therefore unsurprising that commentators in this context would be sceptical of the likelihood that litigation investors would rigorously screen potential claims. But the argument is also made in the context of English and Australian litigation (particularly Australian class actions).⁸²

The common retort is that this is implausible: funders carefully select cases and perform extensive due diligence, and it would be irrational to fund an unmeritorious claim given that funding is provided on a non-recourse basis.⁸³ However, a funder's due diligence process relies on the accuracy of the information provided by the claimant, and a claimant with a weak case has little incentive to fully disclose that fact. Further, if weaknesses in the case become apparent during the course of litigation, there might be a question about the funder's ability to alter the course of the litigation – either by terminating the funding, or exercising some degree of control over its progress. These issues are canvassed in detail in Chapter 10.

Whilst there are high-profile examples of funded claims failing because they were obviously unmeritorious,⁸⁴ it is unknown what the root cause of the problems was

⁸¹ Rubin (n 80) 679-80; Abramowicz (n 80) 197.

⁸² See, eg, US Chamber Institute for Legal Reform, *Before the Flood: An Outline of Oversight Options for Third Party Litigation Funding in England and Wales* (2016), 1, 12-16; US Chamber Institute for Legal Reform, *Submission 19 to the Australian Law Reform Commission Inquiry into Class Action Proceedings and Third-Party Litigation Funders* (2018), [3.3].

⁸³ See Chapter 6 as to the usual terms of funding.

⁸⁴ See, eg, *Excalibur Ventures LLC v Texas Keystone Inc* [2016] EWCA Civ 1144; [2016] 6 Costs LO 999. See also *Chevron Corp v Donziger* 974 F Supp 2d 362 (SDNY 2014), 474-9 as to Burford's ill-fated investment in a claim against Chevron.

in these cases (for example, whether the difficulties in the case were, or should have been, apparent to the funder from the outset, or the extent to which the funding agreement would have permitted the funder to terminate its funding). There is little empirical evidence indicating that unmeritorious funded claims are widespread.

There is, however, some economic analysis. Lysaught and Hazelgrove contend that, with time, litigation investment is likely to increase speculative litigation – the inflow of capital into the litigation funding market will diminish returns, which will in turn force funders to invest in more risky cases in order to maintain investment returns.⁸⁵

Kidd suggests that a net increase in litigation is likely to lead to more errors in the process of screening by courts.⁸⁶ If this were true, however, it would be equally true of any initiative which improved access to the court. Further, and as Silver observes, the claim that funding encourages frivolous litigation must also be true of insurance, as an insured is a more attractive defendant.⁸⁷

There is, however, good reason to be sceptical of any concern about frivolous claims. If impecunious claimants are unable to litigate, or forced into settlements on unfair terms because they cannot afford to litigate to judgment, then that will encourage frivolous *defences*. It is entirely rational for a defendant faced with an impecunious claimant to refuse to pay, even if the claimant has a strong claim.

In the absence of litigation funding, a defendant is the only person who can (in effect) put a value on a cause of action and purchase it, through settlement.⁸⁸ A

⁸⁵ Lysaught (n 17) 662.

⁸⁶ Kidd (n 17) 628-9.

⁸⁷ Silver (n 1) 634.

⁸⁸ Stephen Gillers, 'Waiting for Good Dough: Litigation Funding Comes to Law' (2010) 43 Akron Law Review 677, 683. In economic terms, this is a monopsony: see Vicki Waye, *Trading in*

defendant has no incentive to compensate a claimant who has no capacity or appetite for litigation cost and/or risk. If the defendant refuses to compensate, the claimant has no redress.

In summary, therefore, concern about frivolous claims ought to be balanced against concern about frivolous defences. There is little evidence in the Australian and English funding markets of difficulties caused by unmeritorious claims.

Conclusion

Some criticism of litigation funding stems from a more general view that litigation is undesirable. For the reasons explained above, hostility to litigation is difficult to defend. Beyond the litigation funding context, it is also observed in the context of promoting ADR, and other initiatives which skew incentives away from commencing or continuing litigation.

This thesis adopts the view that litigation – whilst undesirable in many respects for the individual litigant – is socially beneficial. As such, there is no reason to criticise litigation funding on the basis that it has a tendency to increase litigation. There is also little reason to be concerned that these additional claims will be of lower ‘quality’ because of abuse of process or lack of merits.

Legal Claims: Law, Policy & Future Directions in Australia, UK & US (Presidian Legal Publications 2008).

CHAPTER 4: IS LITIGATION FUNDING INCONSISTENT WITH SOME ASPECT OF THE CIVIL JUSTICE SYSTEM?

Introduction

In Chapter 2, I identified that there were four policy concerns which underpinned the modern doctrine of maintenance and champerty (and the remaining concerns about litigation funding). This chapter addresses the second: a concern about the prospect of a third party being involved in litigation. It will be seen that this concern is consonant with a view of civil justice that prioritises party autonomy. But in the modern civil justice system, this concern is misplaced.

What is the objection?

Concerns about the presence of third parties in the litigation process

As was identified in Chapter 2, early case law concerning maintenance and champerty identified the prospect of third parties ‘intermeddling’ in litigation as a mischief against which the doctrines protected. In this vein, Lord Esher MR identified the public policy concerns thus:¹

it seems to have been thought that litigation might be increased in a way that would be mischievous to the public interest if it could be encouraged and assisted by persons who would not be responsible for the consequences of it, when unsuccessful.

In this passage, concern about third party involvement is mixed with concern about an increase in litigation, or encouraging litigation.

¹ *Alabaster v Harness* [1895] 1 QB 339 (CA), 342.

It is common to find judicial statements to the effect that the mischief of litigation funding is the ‘officious intermeddling’ in litigation of a third party with no ‘legitimate interest’. A classic and often-cited statement of principle is that of Fletcher Moulton LJ in 1908. His Lordship considered that much of the law of maintenance was, by then, ‘obsolete’ – but that the remaining prohibitions were intended to prevent:²

... wanton and officious intermeddling with the disputes of others in which the defendant has no interest whatever, and where the assistance he renders to the one or the other party is without justification or excuse.

Modern case continues to reveal concern about third party involvement.³ Even on the current state of the law, in which litigation funding agreements are usually permissible, courts continue to refer to the need for the funder to have a ‘justification’ or ‘excuse’ for intervening in litigation – with no clear definition of what that means.

In *Giles v Thompson*,⁴ Lord Mustill, in an often-cited passage, stated:

... all the aspects of the transaction should be taken together for the purpose of considering the single question whether... there is wanton and officious intermeddling with the disputes of others in where [sic] the meddler has no interest whatever, and where the assistance he renders to one or the other party is without justification or excuse.

Whatever officious intermeddling means, one might assume that it is a different vice to that of ‘trafficking’ – which connotes an objection to the commodification of a cause of action. However, in *Stoczina Gdanska v Latreefers*, the concepts of

² *British Cash and Parcel Conveyors Limited v Lamson Store Service Company Limited* [1908] 1 KB 1006 (CA), 1014, see also 1013 as to the law of maintenance being ‘to a large extent obsolete’. The identification of ‘intermeddling’ as the relevant mischief is not unique to Fletcher Moulton LJ: See, eg, *Neville v London 'Express' Newspaper Limited* [1919] AC 368 (HL), 382 (Lord Finlay LC); see also *Trendtex Trading Corporation v Credit Suisse* [1982] AC 679 (HL), 694 (Lord Wilberforce).

³ See, eg, *Clairs Keeley (A Firm) v Treacy and Others* [2004] WASCA 277; (2004) 29 WAR 479, [124]-[125];

⁴ *Giles v Thompson* [1994] 1 AC 142 (HL).

intermeddling and trafficking were combined by the Court of Appeal, in a manner which creates confusion about the nature of officious intermeddling.⁵

Abuse of the court's process can take many forms and may include a combination of two or more strands of abuse which might not individually result in a stay. Trafficking in litigation is, by the very use of the word "trafficking", something which is objectionable and may amount to or contribute to an abuse of the process. We think that it is undesirable to try to define in different words what would constitute trafficking in litigation. It seems to us to connote unjustified buying and selling of rights to litigation where the purchaser has **no proper reason to be concerned with the litigation. "Wanton and officious intermeddling with the disputes of others in which they [the funders] have no interest and where that assistance is without justification or excuse" may be a form of trafficking in litigation.** [emphasis added]

This passage raises the issue of commodification, but clearly also third party involvement. More recently, the Court of Appeal in the leading case of *Arkin v Borchard*, identified that the level of control exerted by the funder was critical to the distinction between a 'champertous' (unacceptable) and a 'non-champertous' (acceptable) agreement.⁶ Specifically, the Court stated that an unobjectionable funding agreement would be one which would⁷

... leave the claimant as the party primarily interested in the result of the litigation and the party in control of the conduct of the litigation.

The question of third-party control therefore continues to be important.⁸

⁵ *Stocznia Gdanska SA v Latreefers Inc* [2001] 2 BCLC 116 (CA) [61].

⁶ These terms were used at *Arkin v Borchard Lines (Nos 2 and 3)* [2005] EWCA Civ 655; [2005] 1 WLR 3055 [40], [43].

⁷ *ibid* [40] (emphasis added).

⁸ *Davey v Money* [2019] EWHC 997 (Ch), [76].

Inconsistency

This criticism entails an assertion (sometimes unexpressed) about the proper features and role of the civil justice system. If third party control of litigation is undesirable as a matter of principle, then presumably this is because party control of litigation is an important or desirable feature of the civil justice system. This point was expressed clearly by the minority in *Fostif*, who stated:⁹

The purpose of court proceedings is not to provide a means for third parties to make money by creating, multiplying and stirring up disputes in which those third parties are not involved and which would not otherwise have flared into active controversy but for the efforts of the third parties, by instituting proceedings purportedly to resolve those disputes, by assuming near total control of their conduct, and by manipulating the procedures and orders of the court with the motive, not of resolving the disputes justly, but of making very large profits. Courts are designed to resolve a controversy between two parties who are before the court, dealing directly with each other and with the court: the resolution of a controversy between a party and a non-party is alien to this role.

In the next section, I will demonstrate that these values did not arise in a vacuum. Rather, they reflect what I describe as the ‘traditional view of civil justice’ – the value system which guided the civil justice system in the nineteenth and twentieth centuries, prior to the Woolf reforms. The policy reasons underpinning the doctrines of maintenance and champerty are explicable and consistent with this scheme of civil justice.

In later parts of the chapter, I will explain that the values of the civil justice system have changed, as a result of the Woolf reforms in England and their equivalents in Australia, and also because of broader changes in society, such as changes in the

⁹ *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* [2006] HCA 41; (2006) 229 CLR 386 [266] (citations omitted, emphasis added).

perception of the value of litigation. Litigation funding is entirely consistent with the new scheme.

The traditional view of civil justice

An adversarial, party-drive system of private dispute resolution

Sir Jack Jacob's Hamlyn Lectures,¹⁰ delivered in 1986, presented one account of the 'fundamental features' of the English system of civil justice.¹¹ Sir Jack identified, as the first feature, the fact that it was an adversarial system. He considered that several conclusions followed:¹²

... the basic assumptions are that civil disputes are a matter of private concern of the parties involved, and may even be regarded as their private property, though their determination by the courts may have wider, more far-reaching, even public repercussions, and that the parties are themselves the best judges of how to pursue and serve their own interests in the conduct and control of their respective cases, free from the directions of or intervention by the court.

Two themes emerge from Sir Jack's account of the common law system.¹³ First, litigation is treated as an inherently private matter between the parties. Secondly, litigation is controlled by the parties, who can conduct litigation as they see fit; the court has a correspondingly passive role.¹⁴

Jolowicz's account of the civil justice system bears remarkable similarity to that of Jacob. Jolowicz also observed that 'civil litigation should be seen primarily as a

¹⁰ Sir Jack IH Jacob, *The Fabric of English Civil Justice* (Stevens & Sons 1987).

¹¹ It has been adopted by others: see, eg, Robin CA White, *The English Legal System in Action: The Administration of Justice* (3rd edn, Oxford University Press 1999), 233-7.

¹² Jacob, *The Fabric of English Civil Justice* (n 10) 8.

¹³ See also Sir Jack IH Jacob, *The Reform of Civil Procedural Law and other Essays in Civil Procedure* (Sweet & Maxwell 1982), especially 24-5, 62-4, 142-3, 189-91, 204-6, 245-6.

¹⁴ Jacob, *The Fabric of English Civil Justice* (n 10) 5-15 discussed the role of the court.

process for the resolution of disputes'; the rules of court, accordingly, do not contemplate 'that more may be at stake than the interests of the parties to each case'.¹⁵ Zemans, writing about Canadian civil justice, described the civil justice system as a 'highly individualised dispute resolution process in which each litigant must both prosecute and present his or her own case with limited intervention by the court system and no direct involvement by the judiciary'.¹⁶

Jacob considered the implications of the court's passive role, and the correspondingly active role of the parties.¹⁷ The role of the judge was essentially an umpire, called upon not to discover the truth necessarily, but to answer the question put by the parties.¹⁸ A judge could not act of their own volition, save in particular exceptional circumstances.¹⁹ The responsive (rather than proactive) role of the court was explained by Justice in similar terms:²⁰

First, the court has always seen itself as furnishing a public service to litigants, which they are free to use if they wish, and to leave unused if they do not. The court does not regard it as its function to force parties to conduct their disputes in any particular fashion: provided they agree on what is to be done, and it falls within the rules, the court will agree also.

¹⁵ JA Jolowicz, 'On the Nature and Purposes of Civil Procedural Law' in IR Scott (ed), *International Perspectives on Civil Justice: Essays in Honour of Sir Jack IH Jacob QC* (Sweet & Maxwell 1990), 36.

¹⁶ Frederick H Zemans, 'Making the Justice System Balance: Beyond the Zuber Report' in IR Scott (ed), *International Perspectives on Civil Justice : Essays in Honour of Sir Jack IH Jacob QC* (Sweet & Maxwell 1990), 265.

¹⁷ Jacob, *The Fabric of English Civil Justice* (n 10) 7-15.

¹⁸ *ibid* 9. As to the analogy with an umpire, see Sir Frederick Pollock and Frederic William Maitland, *The History of English Law Before the Time of Edward I* (Cambridge University Press 1895), Vol 2, 667 (discussing the position in mediaeval law, but noting that 'This passive habit seems to grow upon them as time goes on and the rules of pleading are developed').

¹⁹ Jacob, *The Fabric of English Civil Justice* (n 10) 9-12.

²⁰ Justice, *Going to Law: A Critique of English Civil Procedure - A Justice Report* (Stevens & Sons 1974) [57].

If control of litigation is placed in the hands of parties, however, it means that lawyers – rather than judges – are the legal professionals who are charged with responsibility for litigation. It is accepted that the claimant alone has the right to choose whether or not to commence proceedings to seek a remedy.²¹ Parties are able to present their case as they choose.²² But if parties are represented, such decisions will be made with the advice of their lawyer. As Jacob explained, the active role given to parties in the adversary system has²³

the effect of greatly increasing the duties and obligations of the lawyers in the civil judicial process and also the dependence of the litigants themselves as well as the courts on their skill, competence and integrity.

The dependence on lawyers may vary with the sophistication and preferences of the client and it is observed that there are a variety of approaches to the extent of sharing control between lawyer and party.²⁴ Critically, though, the lawyer's role is constrained by obligations owed as officers of the court, and legal professional duties, as well as by the rules of court.

In summary, therefore, the traditional view of civil justice perceives civil litigation as overwhelmingly – if not solely – a means of private dispute resolution, with few implications for third parties. It also emphasises the centrality of party control. From this follows the important role of lawyers, and reliance on their skill and honesty.

²¹ *Bremer Vulkan Schiffbau und Maschinenfabrik v South India Shipping Corporation Ltd* [1981] AC 909 (HL), 977E-F.

²² See Ross Cranston, *How Law Works: The Machinery and Impact of Civil Justice* (Oxford University Press 2006), 134 as to the parties' ability to 'to present their side of the matter to what they see as the best advantage'.

²³ Jacob, *The Fabric of English Civil Justice* (n 10) 13.

²⁴ See Cranston (n 22) 196-7 as to the spectrum of different arrangements which exist between party control and lawyer control.

These principles inform specific rules of procedure

The traditional values of the civil justice system may be seen in a variety of specific procedural rules, which give emphasis to the importance of party control and reinforce the private character of litigation. Jacob and Jolowicz identify that the private character of litigation manifests itself in the fact that conceptually, the common law treats the role of the court as being to resolve the dispute between the two parties (albeit that in a system of stare decisis, that has implications for others). For example, courts in common law jurisdictions will not give advisory opinions on legal questions, even where there might be a public interest in clarifying the law – an active controversy between two opponents is required.²⁵

Rules of court and practice also reflect the importance of having the parties – and only the parties – before the court. There are detailed rules for identifying the correct parties, and standing rules which mean that only those with a sufficient interest in the litigation may be heard.²⁶ Even where a judgment has the potential to create a precedent that will radically change the law and thus affect many others, there are limited opportunities for non-parties to put submissions to the court.

Repetitive litigation is generally only prohibited where it involves the same parties or their privies. It is therefore open to the court to make different findings of fact in proceedings involving different parties; findings are only binding between parties.²⁷

²⁵ H F Jolowicz, *Lectures on Jurisprudence* (J A Jolowicz ed, University of London, Athlone Press 1963), 338-40, and the work there cited.

²⁶ See generally Adrian Zuckerman, *Zuckerman on Civil Procedure: Principles of Practice* (3rd edn, Thomson Reuters, Sweet & Maxwell 2013), Chapter 13 'Joining Claims and Parties'.

²⁷ *ibid* [25.66]; Adrian Zuckerman and others, *Zuckerman on Australian Civil Procedure* (LexisNexis Butterworths 2018), [26.69].

More broadly, party control in the common law adversarial system relies heavily on the skill and competence of lawyers. In turn, as Jacob observes, that has led to the creation of a body of law concerned with lawyers' professional and ethical obligations, and rules of court which impose obligations on lawyers. In a system where parties enjoy control and autonomy, these restrictions on lawyers play an exceptionally important role.

We can see that the extensive professional obligations placed on solicitors and barristers is consistent with the traditional scheme of civil justice. It is, I suggest, no coincidence that this traditional view of civil justice coincided in time with a particularly exacting approach to legal professional ethics, which is discussed in the next chapter.

The traditional view of civil justice is consistent with other trends in legal scholarship

The traditional view of civil justice does not exist in a vacuum. It is consistent with prevailing trends in two other areas of legal scholarship.

Private law theory

Private law theory generally assumes a bilateral relationship between the wrongdoer and the injured party. Indeed, Lucy has suggested that this bilateral form may be one of the characteristic features of private law, which distinguishes it from public law.²⁸ One dominant theory is that of corrective justice, most often associated with Weinrib and Coleman. Theories of corrective justice are 'agent-relative'; that is, they contend that the *victim* (and no-one else) must seek a remedy, and the *wrongdoer* (and no-one

²⁸ William Lucy, *Philosophy of Private Law* (Oxford University Press 2007), 22-5, but see also 432-5.

else) must make good the loss they have caused.²⁹ Corrective justice is the duty that arises between those two, to make good the loss.³⁰ Even those theories of corrective justice which accept that a person other than the wrongdoer (such as an insurer) can provide the compensation do *not* allow for the possibility that a person other than the victim will stand in the position of claimant and receive the compensation.³¹

An alternative to corrective justice is a rights-based account such as that of Stevens. This, too, is agent-relative; it requires that the claimant enforce their own right.³²

Economic theories of law also require the victim and wrongdoer to stand in the position of claimant and defendant. The identity of the defendant as the person who pays compensation is necessary to ensure deterrence. The identity of the claimant as the person who receives the compensation is necessary to give the claimant an incentive to enforce the law. It is also important that the amount of compensation received by the claimant is equivalent to the loss they have suffered; over- or under-compensation may cause the claimant to act inefficiently in taking too few, or too many, precautions to avoid the harm themselves.³³

²⁹ Although corrective justice is often explained in the context of tort, Lucy explains how it is more broadly applicable to private law: *ibid* 268-9.

³⁰ See *ibid* 270 and 432-3 for a summary of the key features of corrective justice accounts; see also Ernest J Weinrib, 'The Disintegration of Duty' in M Stuart Madden (ed), *Exploring Tort Law* (Cambridge University Press 2005), 154-6.

³¹ See Mark R Reiff, *Punishment, Compensation, and Law: A Theory of Enforceability* (Cambridge University Press 2005), 170-1; see, for example, Tony Honoré, *Responsibility and Fault* (Hart 1999), 74-5; Neil MacCormick, *Legal Right and Social Democracy: Essays in Legal and Political Philosophy* (Clarendon Press 1982), 214, 217, 226.

³² Robert Stevens, *Torts and Rights* (Oxford University Press 2007), 173.

³³ Richard A Posner, *Economic Analysis of Law* (9th edn, Wolters Kluwer Law & Business 2014), 223. But compare Richard A Posner, *Economic Analysis of Law* (2nd edn, Little, Brown and Company 1977), 143, which treats the identity of the defendant as critical, but the fact that payment is made *to the plaintiff* as a 'detail'; albeit one that is 'important'.

Thus, private law theory treats litigation as essentially a private matter – directed to rectifying the position as between victim and wrongdoer, with these parties (and no others) taking the role of claimant and defendant.

The divide between public and private law

Modern legal scholarship tends to treat private law as taxonomically distinct from public law. Although the civil justice system does, of course, deal with matters of public law, the traditional view of civil justice takes as its paradigm case the private law dispute between private litigants. Thus, a distinction is evident in legal scholarship between public law as ‘the legal realm of collective project pursuit’ and private law being ‘the legal realm of individual project pursuit’.³⁴

The taxonomic distinction is also evident in practice. For example, the prospect of a person other than the wronged party initiating and prosecuting litigation is commonplace in matters of public law, such as criminal and environmental law.

The extent to which courts will encourage litigation or settlement also differs between the two spheres: Jacob has argued that the CPR system ‘offers encouragement to the adjudication of cases which are impressed with aspects of public concern... [but] seek[s] to persuade claimants and defendants to settle where all they want is to assert mere private rights against each other’.³⁵ This manifests in specific rules – for example,

³⁴ Lucy (n 28) 19.

³⁵ Joseph M Jacob, *Civil Litigation: Practice and Procedure in a Shifting Culture* (EMIS Professional Publishing 2001), 19-20; cf Stephen Sedley, ‘Improving Civil Justice’ (1990) 9 *Civil Justice Quarterly* 348, 348-50, who argued (in 1990, before the introduction of the CPR) that commercial law and public law were prioritised by the courts over individual disputes. According to Sedley, commercial law was prioritised in order to maintain London’s status as a leading centre for business (see 349).

one of the criteria for the grant of a protective costs order is that a claim raises issues of ‘general public importance’ in which ‘the applicant has no private interest’.³⁶

Again, the taxonomic divide is consistent with the traditional view of civil justice. Private law disputes are a matter for the parties alone, and only public law disputes engage a broader public interest.

Litigation funding does not fit with the traditional view of the civil justice system

Returning to the criticisms made of litigation funding, and the policy reasons which underpinned the doctrines of maintenance and champerty, we can see that these do not arise in a vacuum. Rather, they are entirely consistent with the values which the civil justice system espoused in the 19th and 20th centuries.

As explained in the previous section, one aspect of the traditional view of civil justice is that the decision whether to litigate – and the conduct of litigation once commenced – is a matter for parties and their lawyers. In the litigation funding context, this leads to two problems when a third party funder is involved.

First, a funder might cause proceedings to be brought ‘which would not otherwise have flared into active controversy’. Litigation funding can therefore be said to challenge the idea that litigation (including the decision to litigate) is essentially a matter of private dispute between the parties.

Secondly, a funder may exert control or influence over the progress of litigation. On the traditional view, parties control litigation and the court is passive. Parties are

³⁶ *R (on the application of Corner House Research) v Secretary of State for Trade and Industry* [2005] EWCA Civ 192; [2005] 1 WLR 2600, [74].

advised by lawyers – but the high level of control and responsibility which is reposed in lawyers in an adversarial system is matched by far-reaching and onerous legal and professional obligations, owed to the court and the client. Funders, on the other hand, owe no such professional obligations to the court or to the litigants.

The civil justice system: an evolving landscape

In the remainder of this chapter, I will demonstrate that these criticisms of litigation funding are misplaced. The modern civil justice system espouses a different set of values and priorities, and litigation funding is entirely consistent with these.

The first observation we can make about the civil justice system is that its features and values are not static, but constantly evolving.³⁷ The constant evolution of the common law civil justice system is best thought of as the product of two influences.³⁸ First, it is the product of historical contingency. The current form of the civil justice system is in large part attributable to events and policy decisions which have built up over several centuries. Secondly, it is the product of what might be described as prevailing social values. Over time, social and intellectual influences have shaped the values which are reflected and supported by the civil justice system.

³⁷ AAS Zuckerman, 'A Reform of Civil Procedure - Rationing Procedure rather than Access to Justice' (1995) 22 *Journal of Law and Society* 155, 161.

³⁸ DJ Galligan, *Law in Modern Society* (Oxford University Press 2007), 20. In this section, I refer extensively to Galligan and Berman. But to similar effect, see also RC van Caenegem, *The Birth of the English Common Law* (2nd edn, Cambridge University Press 1988), 107; Tom Bingham, *The Business of Judging: Selected Essays and Speeches 1985-1999* (Oxford University Press 2000), 375-80.

Changes driven by historical contingency

Many central features of the common law civil justice system are, in reality, largely a product of historical contingency.³⁹ In the early English legal system, developments such as the separation of secular and ecclesiastical law,⁴⁰ the emergence of the concept of the state,⁴¹ the unification of English law, and the development of the writ system,⁴² occurred by reason of political or social forces, or as a by-product of some other change.

The concept of a distinction between ‘the affairs of the government and the affairs of private individuals’ took hold because of political events – the increasing workload of the Council and the Court of Star Chamber in the sixteenth century.⁴³ In fact, the very concept of the rule of law was, in mediaeval times, motivated by the belief that there was *no* fundamental distinction between public and private – the king could be required to account to the court in the same way as his subjects.⁴⁴

More recently, it can be seen that the system of precedent – sometimes said to be a key feature of the common law – did not emerge fully-formed. Treating like cases alike follows naturally from the fact of having uniform rules. But initially, citations would be limited to cases of which the parties’ advocate, or the judge, had had personal

³⁹ See Harold J Berman, *Law and Revolution: The Formation of the Western Legal Tradition* (Harvard University Press 1983) for a detailed treatment of the events, and social forces, which led the modern common law system to have its current form.

⁴⁰ *ibid* 88-119.

⁴¹ Berman (n 39) 275ff.

⁴² *ibid* 445ff.

⁴³ GRY Radcliffe and others, *The English Legal System* (6th edn, Butterworths 1977), 110. Oliver claims that it is of more recent origin, attributing it to the House of Lords judgment in *O’Reilly v Mackman* [1983] 2 AC 237: see Dawn Oliver, *Common Values and the Public-Private Divide* (Butterworths 1999), 80-1.

⁴⁴ Brian Z Tamanaha, *On the Rule of Law: History, Politics, Theory* (Cambridge University Press 2004), chapter 2.

experience.⁴⁵ The system of precedent made a great leap forward when proper reports were made of cases.⁴⁶

The rules of precedent as we understand them in the common law system could only become fully formed when there was a clear hierarchy of courts, which did not take place until the Judicature Acts of 1875, and accurate court reports, which also emerged only in the nineteenth century.⁴⁷ Rules of precedent have continued to evolve since then.⁴⁸ In Australia,⁴⁹ the application of the rules of precedent has changed with growing independence from the United Kingdom. Thus, features of the common law which we today regard as central are, in fact, relatively recent in origin, and can again be said to have occurred because of social contingencies, including developments in technology.⁵⁰

⁴⁵ See Jolowicz *Lectures on Jurisprudence* (n 25) 226-8.

⁴⁶ *ibid* 228-9.

⁴⁷ Carleton Kemp Allen, *Law in the Making* (7th edn, Clarendon Press 1964), 219-30 provides an excellent overview of the development of clear court hierarchy and the emergence of reliable reports. He argues (at 219) that *stare decisis* as it currently exists 'was not, and indeed could not be, settled until the nineteenth century', but notes the debate about the origins of the system of precedent: see 219, footnote 2 and cf Carleton Kemp Allen, *Law in the Making* (2nd edn, Clarendon Press 1930), 149-50. See also Jolowicz *Lectures on Jurisprudence* (n 25) 230.

⁴⁸ In 1963, Jolowicz described the rule that the House of Lords was bound by its own decisions as 'comparatively new', tracing it to *AG v Dean and Canons of Windsor* (1860) 8 HLC 369 and *Beamish v Beamish* (1861) 9 HLC 274: Jolowicz *Lectures on Jurisprudence* (n 25) 231. However, this position has since changed again: in 1966, the House of Lords issued a practice statement which permitted it to deviate from its own decisions in certain circumstances. Between 1966 and 2009, 21 such judgments were issued: Louis Blom-Cooper, '1966 and All That: The Story of the Practice Statement' in Louis Blom-Cooper, Gavin Drewry and Brice Dickson (eds), *The Judicial House of Lords: 1876-2009* (Oxford University Press 2009), 136, 143; Brice Dickson, 'A Hard Act to Follow: The Bingham Court, 2000-8' in Louis Blom-Cooper, Gavin Drewry and Brice Dickson (eds), *The Judicial House of Lords: 1876-2009* (Oxford University Press 2009), 271-2; but cf Michael Beloff, 'The End of the Twentieth Century: The House of Lords 1982-2000' in Louis Blom-Cooper, Gavin Drewry and Brice Dickson (eds), *The Judicial House of Lords: 1876-2009* (Oxford University Press 2009), 239.

⁴⁹ See generally Murray Gleeson, 'The Privy Council - An Australian Perspective' (Address to the Anglo-Australian Lawyers' Society, the Commercial Bar Association and the Chancery Bar Association, London, 18 June 2008); Michael Kirby, 'The Old Commonwealth - Australia and New Zealand' in Louis Blom-Cooper, Gavin Drewry and Brice Dickson (eds), *The Judicial House of Lords: 1876-2009* (Oxford University Press 2009).

⁵⁰ Galligan (n 38) 77.

The same is true of changes in the substantive law. For example, the evolution of the tort of negligence in the nineteenth and twentieth centuries into the tort of ‘majestic pre-eminence’⁵¹ has been driven by a variety of social and economic contingencies: the increased corporatisation of economic activity, and with it the increased incidence of corporate defendants (against whom judges were less reluctant to order damages); a change in social values away from ‘acute individualism’ and apportioning blame in accordance with moral standards, and towards a ‘communitarian approach’ in which public policy guided the standard of care; and changes in trial process which led to the decline of the jury trial.⁵²

Changes driven by evolving social values

Changes in procedural and substantive law have also been driven by changes in social values. The decline of the jury system led to the reconceptualization of tort and contract. In the case of negligence, it led to a decrease in the ‘fragmentation’ of causes of action, and the trend towards a general duty of care.⁵³ In the law of contract, it led to attempts ‘to fit the Common law into an apparently rational framework’ and clarify areas which ‘had formerly been allowed to remain fuzzy’.⁵⁴ These developments, together with the abolition of forms of action, paved the way for tort law to be treated as a unified corpus, rather than as a disparate collection of individual rights. This unification and systemisation of law probably reached its zenith with the judgment of Lord Atkin in *Donoghue v Stevenson*, which reconceptualised tort law around

⁵¹ MA Millner, *Negligence in Modern Law* (Butterworths 1967), 227.

⁵² D Ibbetson, ‘The Tort of Negligence in the Common Law in the Nineteenth and Twentieth Centuries’ in EJM Schrage (ed), *Negligence: The Comparative Legal History of the Law of Torts* (Duncker & Humblot 2001).

⁵³ David Ibbetson, *A Historical Introduction to the Law of Obligations* (Oxford University Press 1999), 188-9.

⁵⁴ *ibid* 220.

motivating principles, rather than discrete causes of action.⁵⁵ In turn, this unification and systemisation has inspired more philosophical thought about the legal system. The vast literature on the purpose and values of the private law system only makes sense because the law has come to treat itself as having an internal purpose and logic.⁵⁶

An obvious recent example of this trend is the focus on human rights in modern legal thinking, and in public discourse about law. Friedman explains that human rights values have progressed from being merely a social force, to effecting change in the ‘legal culture’ – that is, human rights values have given rise to ‘concrete demands and expectations’ about what the law will do.⁵⁷

Contemporary discourse in legal theory about the position of individuals with respect to each other and the state is dominated by the concept of rights.⁵⁸ Indeed, Gearey et al contend that contemporary ‘common law must be understood as an articulation of human rights and open justice’.⁵⁹

Friedman, in discussing the key features of contemporary ‘legal culture’, observes that ‘It is part of modern legal culture to believe that law (and society) should treat people as equals – regardless of gender, race, religion, caste.’⁶⁰ He goes so far as

⁵⁵ Galligan (n 38) 77 identifies the ‘decline of the writ-system’ and the growth of a general tort of negligence as opposed to ‘specific torts with strict rules’ as examples of the common law shifting when ‘rules became too rigid, or were no longer reasonable expressions of social relations and practices’.

⁵⁶ Cf Lucy (n 28) 22; see also Weinrib (n 30) 143-5.

⁵⁷ Lawrence M Friedman, ‘The Place of Legal Culture in the Sociology of Law’ in Michael Freeman (ed), *Law and Sociology: Current Legal Issues Volume 8* (Oxford University Press 2006), 189-90. One example, discussed by Friedman at 193-5, is the social changes that – via a change in the legal culture – led to radical changes in family law. See also W Friedmann, *Law in a Changing Society* (2nd edn, Stevens & Sons 1972), 25-8 as to the ‘interaction between the articulation of public opinion and the legislative process’.

⁵⁸ Galligan (n 38) 209-10; as to disapproval of this phenomenon, see P A Keane, ‘Access to Justice and other Shibboleths’ (JCA Colloquim, Melbourne, 10 October 2009), 13.

⁵⁹ Adam Gearey, Wayne Morrison and Robert Jago, *The Politics of the Common Law: Perspectives, Rights, Processes, Institutions* (2nd edn, Routledge 2013), foreword.

⁶⁰ Friedman, (n 57) 196.

to say that this has changed the legal *structure* – that is, the ‘settled, durable, institutional aspects of a legal system’,⁶¹ by, for example, changing the role of the courts.

This sociological observation about the fit between law and society can be seen to be consistent with observed practice in England. For example, the Human Rights Act has changed the role of the court in relation to judicial review. It has also provided new standards against which the civil justice system can be judged.⁶²

The traditional view of civil justice: a product of historical contingencies, and the social values of its time

The traditional view of the civil justice system is also a product of its time: it can be seen to have been influenced both by broader political values and by external social pressures and reforms. As to the former, Zemans argued that it reflects prevailing Western political values: ‘an individualistic, liberal view of society’ in which ‘the foremost concern... is the protection of individual rights’.⁶³ Uzelac also makes the argument that the ‘conflict resolution’ model of civil litigation – in which litigation is a means of private dispute resolution, controlled by the parties – reflects a broader political ideology. He explains:⁶⁴

⁶¹ *ibid* 198-9.

⁶² For example, in *Coventry v Lawrence* [2015] UKSC 50; [2015] 1 WLR 3485, the Supreme Court considered the compatibility of the CFA regime which existed prior to the Legal Aid, Sentencing and Punishment of Offenders (LASPO) Act 2012 (UK) (‘LASPO’) with human rights norms.

⁶³ Zemans (n 16) 265. See also Chief Justice Murray Gleeson, ‘Some Legal Scenery’ (Judicial Conference of Australia, Sydney, 5 October 2007), 11. Zemans described the civil justice system as a ‘highly individualised dispute resolution process in which each litigant must both prosecute and present his or her own case with limited intervention by the court system and no direct involvement by the judiciary’: see 265.

⁶⁴ Alan Uzelac, ‘Goals of Civil Justice and Civil Procedure in the Contemporary World’ in Alan Uzelac (ed), *Goals of Civil Justice and Civil Procedure in Contemporary Judicial Systems: Ius*

The exclusive focus of civil justice on the conflict resolution goal was historically associated with the liberal states of the nineteenth century.... As an instrument of the reactive liberal state, civil justice had to provide its services in the way that would ensure a minimum of intervention. Just as the *laissez-faire* economy refrains from intervening in the business transactions between private parties, the liberal system of civil justice refrains from intervening in the legal transactions of private law, by giving the maximum powers to the litigants.... The end result, in the interest of putting an end to the conflict, must therefore be final – *res iudicata* – but it affects only the parties (*facit ius inter partes*), and is none of anybody else’s business.

The *Judicature Acts* which entrenched many of the features of the traditional view of the civil justice system were, themselves, a break from the past. Jacob has observed that the civil justice system which had existed in 1800 was ‘completely replaced by an entirely new system’;⁶⁵ the change arose because of⁶⁶

the conjunction of three factors, the objective social conditions, the theoretical spark, and a sustained and informed public opinion which together call for change.

The changes effected by the Judicature Acts of the 1870s (and the civil justice reforms in the twentieth century which preceded the Woolf reports) were motivated by ‘a specific legal philosophy or theory of justice.’⁶⁷ That reform of the civil justice system ought to have an overall guiding objective was first identified by the Law Reform Commission in 1852.⁶⁸ The chosen objective was the concept of ‘substantive

Gentium Comparative Perspectives on Law and Justice, Volume 34 (Springer International Publishing 2014), 7.

⁶⁵ Jacob *The Reform of Civil Procedural Law* (n 13) 206; see generally 204-8. See also ‘The Judicature Acts 1873-1875: Vision and Reality’ at 301 and following in the same volume.

⁶⁶ *ibid* 207.

⁶⁷ John Sorabji, *English Civil Justice after the Woolf and Jackson Reforms: A Critical Analysis* (Cambridge University Press 2014), 1-2.

⁶⁸ *ibid* 52; for a lengthier exposition, see JA Jolowicz, *On Civil Procedure* (Cambridge University Press 2000), 357-9.

justice'.⁶⁹ This entailed the idea, adopted from courts of equity, that courts ought to do complete justice between all affected parties.

Thus, the state of English civil justice between the Judicature Acts and the Woolf reforms was motivated by an explicit commitment to a particular value: substantive justice. This in turn had arisen out of social pressures in the early- to mid-nineteenth century.

The traditional view of civil justice is, therefore, not fixed and immutable. It is a product of its time, and then-prevailing social values.

Summary: a system of constant evolution

In summary, the constant theme of the common law civil justice system has been that it is moulded by external forces, including changing social conditions and values, and technological developments. A contemporary account of the central features and values of the civil justice system must therefore account for prevailing social conditions and values.

Identifying the modern values of the civil justice system

We can identify a series of values which have influenced the modern civil justice system. Some – such as the Woolf reforms – are internal to the civil justice system. Others – such as the increased prevalence of market forces – are aspects of broader social trends.

⁶⁹ Also referred to as 'achievement of justice in the individual case; substantial or real justice; complete justice; a correct decision; rectitude of decision; justice on the merits': see Sorabji (n 67) 2.

The Woolf and Jackson reforms: the civil justice system adopts managerial culture

Sorabji has explained that the Woolf and Jackson reforms ought to be conceived of as a radical new theory of justice, which effect a paradigm shift in the civil justice system.⁷⁰ Specifically, the new guiding principle is proportionate justice.⁷¹ Thus, rectitude of decision making is but one aspect of justice; justice also requires ‘the pursuit of economy, efficiency, expedition, equality and proportionality’.⁷² This change was effected in two ways: first, by the introduction of the overriding objective,⁷³ and secondly, by making structural changes in the rules, such as introducing active case management and procedural tracks.⁷⁴ The overall aim was the achievement of accessibility to the court for all.⁷⁵ The Woolf reforms have been followed to a large extent in Australian jurisdictions.⁷⁶ The commitment to ‘substantive justice’ as the pre-eminent value of the civil justice system has been expressly rejected by the Woolf reforms.⁷⁷

⁷⁰ Sorabji (n 67). At Chapter 4, Sorabji considers the claim that the Woolf reforms effect a ‘business as usual approach’, seeking to improve the civil justice system within the paradigm of substantive justice. However, in Chapters 5 and 6, he persuasively explains why the better view is that proportionate justice is a new theory of justice. See also ‘Procedure’ in Cranston (n 22) especially 146-7 and 150-1.

⁷¹ *Zuckerman on Civil Procedure* (n 26) [1.5]-[1.13].

⁷² Sorabji (n 67) 3.

⁷³ *ibid* 164-5.

⁷⁴ *ibid* 182-96.

⁷⁵ *ibid* 164.

⁷⁶ *Zuckerman on Australian Civil Procedure* (n 27) Chapter 1.

⁷⁷ See the discussion in Sorabji’s work under the headings ‘The traditional view of civil justice’ and ‘The Woolf reforms: the express adoption of new guiding principles in the civil justice system’.

One aspect of these procedural reforms is that the parties' control of litigation may be fettered by the court, which must take a greater role in directing the conduct of litigation in order to promote the goals of efficiency and proportionality.⁷⁸

Thus, two important changes have been effected to the civil justice system by the recent procedural reforms. The unifying theory of the civil justice system – i.e. substantive justice – has been challenged, if not entirely replaced by a theory in which managerial values are pre-eminent. Further, to achieve that end, specific aspects of the traditional view of civil justice have been undermined: most obviously, party control and autonomy in the conduct of litigation.

Managerial culture

In order to effect the proportionate allocation of resources which was the central plank of the Woolf reforms, it was necessary for judges to adopt a managerial role, which required not only specific rule changes, but also cultural change.⁷⁹ It has been suggested that the radical changes to the civil justice system effected by the Woolf reforms are a product of a broader cultural trend towards managerial culture.⁸⁰

Beyond the Woolf and Jackson reforms, a further obvious example of a managerial approach is the introduction of class actions in Australia, and the nascent moves towards collective proceedings in England. The introduction of class actions in Australia was expressly motivated not only by the need to provide redress for small claims, but also to promote efficiency even where each individual claim would be

⁷⁸ Sorabji (n 67) 136, 184-7.

⁷⁹ Zuckerman, 'A Reform of Civil Procedure – Rationing Procedure rather than Access to Justice' (n 37) 171-4.

⁸⁰ Jacob, *Civil Litigation: Practice and Procedure in a Shifting Culture* (n 35) 2-3, 39, 81-2, 107.

economic.⁸¹ Of course, class actions necessarily decrease the autonomy of the individual party. In providing more routes for collective redress, therefore, we can see an explicit decision to value managerial culture – i.e. the value of efficiency – over party autonomy, a value which was pre-eminent in the traditional view of civil justice.

Access to justice as a human right

Earlier in this chapter, it was explained that human rights discourse has affected and influenced the modern civil justice system. The right of access to justice is a principle of longstanding, with constitutional force. But the advent of human rights discourse has led to greater emphasis on this right. The importance of access to the court as a common law right, and, in England, under Article 6, will be addressed further in Chapter 7.

For present purposes, it is sufficient to note two matters. First, access to the court has, in itself been recognised as a human right.⁸² Secondly, access to justice is necessary for the enjoyment of all other rights;⁸³ a ‘right’ which cannot be enforced is a thing of little value.

The introduction of market forces to the legal profession

In the last forty years, there has been a sustained effort by governments to expose the legal profession to the rigours of market forces. Rules and laws regulating the legal profession have been amended with a view to enhancing competition between legal

⁸¹ Commonwealth of Australia, *Hansard* (1991), 3174-3175 (Duffy).

⁸² See generally Joseph M Jacob, *Civil Justice in the Age of Human Rights* (Ashgate 2007); see, eg, *Golder v UK* [1975] ECHR 1.

⁸³ Cranston (n 22) 37, although note at 4-5 his comments about the virtues of alternative dispute resolution.

practitioners, and between the legal profession and other professions – these changes will be addressed in detail in the next chapter.

For present purposes, though, it is sufficient to note two things. First, the introduction of market forces to the legal profession in England and Australia has been a result of deliberate policy choices of successive governments and/or regulators.⁸⁴ Thus, the mercantilisation of the legal profession is the product of external social pressures on the legal profession. Secondly, the move towards a more efficient market for the provision of legal services has been coincided with a diminution in the provision of civil legal aid funds.

The effect of these changes has been that the cost of legal services for civil litigation are now borne privately (rather than provided for by the state), and are subject to market forces.

The breakdown of private and public spheres of law

Treating the civil justice system as concerning essentially private matters between disputants – as in the traditional view of civil justice – entails drawing a sharp line between civil justice on one hand, and, on the other hand, criminal justice and other areas of public law. In the public and criminal law spheres, it is well-accepted that a person other than the wronged party (principally the State) may initiate and control litigation.

As explained earlier, the divide between public and private law is a relatively recent historical contingency. Originally, all law was essentially private law: those who were wronged took steps to seek justice, which was often in a form which we would

⁸⁴ See generally John Peysner, *Access to Justice: A Critical Analysis of Recoverable Conditional Fees and No Win No Fee Funding* (Palgrave Macmillan 2014).

equate to a modern tortious remedy.⁸⁵ In time, distinct principles of criminal law developed, but it was still the victim who prosecuted crime.⁸⁶ It was not until the middle of the 19th century that crime was investigated and prosecuted by the State.⁸⁷

Since the mid twentieth century, the position has changed again. Many observers of Western legal systems have observed a substantial expansion of the state into areas which were traditionally the concern of private law, or outside law's remit altogether.⁸⁸ For example, contract law has been affected by consumer protection and fair trading regulations.⁸⁹ Environmental and labour laws place disparate restrictions on the commercial activities of individuals and corporations. The life of corporations is regulated in a variety of ways – for example, there are continuous disclosure obligations, prohibitions against anti-competitive behaviour, and rules for the internal regulation of corporations. One example, which will be referred to in Chapter 8, is the regulation of financial services providers. As will be seen, this is an area in which there exists an extremely extensive consumer protection regime, which is supported by the creation of new causes of action, and even tailored dispute resolution processes.

The increasing intrusion of the state into diverse fields of human endeavour has a variety of consequences. First, it challenges the liberal view of a laissez-faire state,

⁸⁵ Radcliffe (n 43) 6-7, 34-5, 194-5; Berman (n 39) 53-6. See also Jolowicz *Lectures on Jurisprudence* (n 25) 322, 344.

⁸⁶ See generally John H Langbein, *The Origins of Adversary Criminal Trial* (Oxford University Press 2003), 2-15.

⁸⁷ Radcliffe (n 43) 195.

⁸⁸ See, eg, Jacob *The Reform of Civil Procedural Law* (n 13) 153; Berman (n 39) 33-5; Gleeson, 'Some Legal Scenery' (n 63) 14. Galligan (n 38) 224 observes that there is a tension between law's role in securing social relations (for example, through contract law) – which expresses liberal values – and its role in regulation. The latter involves the active pursuit of social goals, which may well diverge from current social practice (see 213). Berman considers that this phenomenon – driven by social forces – is so significant that it represents a challenge to the entire Western legal tradition: Berman (n 39) 33.

⁸⁹ See, eg, Competition and Consumer Act 2010 (Cth), especially Schedule 2 – the Australian Consumer Law; Consumer Rights Act 2015 (UK).

which will intervene only when called upon.⁹⁰ Secondly, it is incumbent on the state to enable these new rights to be enforced. A right which cannot be enforced is no right at all, and it is the responsibility of the state which creates the rights to ensure that the declared law is consistent with practice.⁹¹

Most importantly, it diminishes any divide which might have existed between public and private law.⁹² When parties to a contract are subject to legislation concerning what the fair terms might be,⁹³ for example, how should we characterise that obligation and right? The legislation in question has been promulgated by the State, presumably because it serves a public interest to regulate contracts in that manner. However, the legislation also serves to protect the weaker party to the bargain. Its utility is that it can be used by the weaker party in civil proceedings, which the weaker party will bring for their own benefit, to recover their loss. Is it still accurate to characterise such a dispute as being of a private nature?⁹⁴

The divide between public and private breaks down further at the point of enforcement. Many of the new rights and obligations created by legislation are enforced by the State; many are able to be enforced by individuals with standing. Some rights can be enforced by either an administrative agency *or* an affected individual. If a company has breached its obligations of continuous disclosure to the market, for example, proceedings might be commenced by the regulator, or by a person who has suffered loss as a consequence of the breach.⁹⁵ The identity of the person commencing

⁹⁰ See the text accompanying footnotes 63 to 64 above.

⁹¹ This arises from the rule of law: see the discussion in Chapter 3.

⁹² Berman (n 39) makes this point at 38. See generally his explanation at 33-8.

⁹³ See above n 89.

⁹⁴ Ronald Dworkin, *A Matter of Principle* (Clarendon Press 1985), 73 makes a similar point.

⁹⁵ Corporations Act 2001 (Cth), ss 674 and 675 (creation of offence), and s 1317HA (creation of private remedy); see also s 1317J ('Who may apply for a declaration or order').

proceedings – State or private individual – is contingent. Even where the state initiates proceedings, it may do so for the benefit of private individuals, or – alternatively – for punitive, law-enforcement purposes.⁹⁶ A similar position exists in respect of consumer protection laws.⁹⁷ How, then, are we to distinguish between private and public interests? How can the characterisation of civil justice as being the resolution of private disputes be maintained?

Modern legal scholarship tends to distinguish between public and private law; indeed, the field of private law theory, referred to above, is premised on there being a corpus identifiable as ‘private law’. But there are competing conceptual views. For example, Austin, Duguit and Kelsen all rejected the idea that the two fields were essentially different.⁹⁸ Berman observes that the distinction between the two – and the creation of discrete bodies of law within each sphere – ‘was a product of the legal thought of the eighteenth-century Enlightenment’.⁹⁹ Indeed, scholars who seek to identify what characteristics distinguish public and private law have struggled.¹⁰⁰ Oliver has persuasively challenged the distinction between public and private, arguing that more is to be gained by considering the similarities than the differences. She argues that the two spheres are:¹⁰¹

concerned in similar if not identical ways, with three projects: to protect the interests of individuals in their autonomy, dignity, respect, status and security; to control exercises of power; and to promote democracy and

⁹⁶ See, eg, *ibid* ss 1317M, 1317N and 1317P.

⁹⁷ See, eg, Competition and Consumer Act 2010 (Cth), Schedule 2, ss 224 and 237(1)(b).

⁹⁸ Jolowicz *Lectures on Jurisprudence* (n 25) 156, 320-7, see also 146-7.

⁹⁹ Berman (n 39) 35.

¹⁰⁰ See, eg, Jolowicz *Lectures on Jurisprudence* (n 25) 320-7; Oliver (n 43) 22-9; Lucy (n 28) 12-20, 432-4.

¹⁰¹ Oliver (n 43) preface; see also 11, 273.

citizenship both in the public or political sphere and in the private sphere.

Oliver claims that public and private law use equivalent ‘techniques’ for achieving these aims. For example, she observes that the concept of reasonableness permeates both public law (in the context of administrative review) and tort. Similarly the restraints placed on the exercise of public powers have important similarities to the regulation of fiduciary relationships in equity.¹⁰²

Oliver also contends that common values motivate both areas of law, specifically: ‘autonomy – in the sense of freedom of action – dignity, equal respect, status and security’.¹⁰³ More specifically, she claims that family, state/citizen and employment relationships have evolved in the twentieth century; in response, law has furthered these common values by, for example, protecting the interests of the weaker party across each of those categories of law, and restraining the exercise of power by the stronger party.¹⁰⁴ To Oliver’s examples could be added contract law and corporate law.

In summary, any divide between public and private is a historical contingency. To the extent that there ever was a dividing line, it is now blurred. In any event, many theorists have struggled to find a persuasive set of criteria for distinguishing the two spheres.¹⁰⁵

¹⁰² *ibid* 11.

¹⁰³ *ibid* 56; see generally chapter 3.

¹⁰⁴ *ibid* chapters 6 to 8.

¹⁰⁵ See, eg Jolowicz *Lectures on Jurisprudence* (n 25) 320-7; *ibid* 22-9; Lucy (n 28) 12-20, 432-4.

Implications for the role of litigation funding in the civil justice system

For centuries, the doctrines of maintenance and champerty required parties to fund their own litigation, or to forego claims. There were always difficulties with such a rule.

First, as a matter of practicality, the rule prevented the impecunious from accessing the courts. As the exceptions grew (in response to this), the law became increasingly complex, and also anomalous (for example, the position of an insurer, as a third party who is able to fund and control litigation, is anomalous).

Secondly, as a matter of principle, it was also difficult to reconcile with the principle of freedom of contract.¹⁰⁶ It is a matter of ‘paramount public policy’ that¹⁰⁷

men of full age and competent understanding shall have the utmost liberty of contracting, and that their contracts when entered into freely and voluntarily shall be held sacred and shall be enforced by courts of justice.

The circumstances in which a court will refuse to enforce a contract on the grounds of public policy are relatively rare.¹⁰⁸ In the absence of the abuses of process which threatened the mediaeval courts, it is difficult to articulate what the problem is.

There is also good reason to question why it was ever important, as a matter of principle, that parties who are unfortunate enough to have been drawn into litigation ought to pay for their own legal costs. When claimant and defendant disagree about their legal obligations towards each other, there is no alternative to litigation; indeed, the very purpose of the civil justice system is to create a mandatory, state-backed

¹⁰⁶ As to which, see generally HG Beale, *Chitty on Contracts* (33rd edn, Sweet & Maxwell 2018), [1-031]-[1-040].

¹⁰⁷ *Printing and Numerical Registering Co v Sampson* (1875) LR 19 Eq 462, 465.

¹⁰⁸ Beale (n 106) [16-047]-[16-174].

alternative to self-help.¹⁰⁹ Indeed, if we consider that one benefit of the civil justice system is that all citizens can order their affairs in the shadow of the law, litigants are particularly unlucky in having failed to enjoy this benefit. Litigants have found it necessary to go to court to avoid the sort of injustice which most of the time, is forestalled because of the prophylactic effect of the civil justice system.¹¹⁰ Further, by litigating, litigants provide the claims which are the lifeblood of the common law system.¹¹¹ Given litigants' lack of choice whether to litigate, the disadvantages of doing so, and the public benefit of litigation, one might seriously question the justice of requiring litigants to self-fund.¹¹²

However, until relatively recently, one virtue of maintenance and champerty was that it was, at least, consistent with the broader scheme of the civil justice system: namely, the values of party control, and the private nature of the civil justice system. Modern developments have made the doctrines more difficult to uphold.

How does litigation funding fit within this alternative view of the civil justice system?

In Chapter 2, I explained that the doctrines of maintenance and champerty historically prohibited litigation funding, and continue today to provide the outer limits of permissible funding agreements. I explained that these doctrines have been driven by

¹⁰⁹ Frederick Wilmot-Smith, *Equal Justice: Fair Legal Systems in an Unfair World* (Harvard University Press 2019), 175-9, and see 24-5 for an explanation of the 'burdens of legality'.

¹¹⁰ *ibid* 183-4; Jeremy Bentham, 'A Protest Against Law Taxes' in Michael Quinn (ed), *Writings on Political Economy*, vol 1 (Clarendon Press 2016), 280.

¹¹¹ Wilmot-Smith (n 109) 183.

¹¹² Indeed, following this reasoning, Wilmot-Smith proposes that justice requires state funding of legal costs via taxation: *ibid* Chapter 9.

themes of protecting party autonomy, preventing the involvement of third parties, and regarding litigation as undesirable.

But these themes did not exist in a vacuum. Rather, they are consistent with the view of civil justice which was dominant in the 19th and 20th centuries.

In the previous section, it was identified that the modern civil justice system is being influenced and moulded by four trends:

- An increased emphasis on human rights. One aspect of this is the right of access to justice, which (as explained in Chapter 3) is both a right and a value which permeates the civil justice system.
- The mercantilisation of the legal profession.
- The imposition of managerial culture, in which litigation is conducted proportionately, and courts actively manage (at the expense of complete party control).
- The expansion of the State, creating new rights, and diminishing the divide between private and public law, a division which is historically contingent and difficult to draw in any event.

It will be observed that the first and fourth trend are also inconsistent with a suggestion that litigation is to be avoided (which was addressed in Chapter 3).

Earlier in this chapter, it was explained that the distinction between public and private litigation can be contingent: the same facts might give rise to a variety of rights and obligations, in respect of which different persons might initiate proceedings. There

is no serious suggestion that the State, in investigating and prosecuting regulatory offences, is ‘stirring up litigation’, or engaging in ‘officious intermeddling’.¹¹³

Further, drawing on the discussion about the importance of enforcement of legal rights to upholding the rule of law, there is little basis for suggesting that court resolution of private law matters is any less important to the public interest than court resolution of public law matters. The concern that third-party funding ‘stirs up litigation’ is therefore difficult to sustain, if it is accepted that the divide between public and private law is open to challenge.

Secondly, the role of litigation funders as third parties – which, as explained in Chapter 1, gives rise to questions about the permitted level of control or influence over litigation – can also be thought of afresh. In public law litigation, it is well-accepted that third parties may initiate proceedings, and fund. Again, if the distinction between public and private law is open to challenge, then we ought also to question why private law cannot more readily accommodate the presence of a third party.

Thus, we can see that the emergence of litigation funding is consistent with broader values and trends in the civil justice system.

Litigation funding enables law to be enforced. It does so in a variety of ways, depending on the context in which it is used. When litigation funding is used by the impecunious, or those who have no appetite for litigation, it enables the prosecution of causes of action which would otherwise not be brought (and therefore provides remedies for wrongs which would otherwise be unremedied). When litigation funding is used in a class action context, it facilitates the enforcement of rules which might

¹¹³ Of course, one might challenge whether the *substance* of the law ought to intrude so far into matters which were historically private: see, eg, Galligan (n 38) 224. But that concerns the content of the substantive law, not its enforcement.

otherwise be breached with impunity, owing to the fact that there are many small losses – or, where the individual losses are large, it enables those claims to be prosecuted more efficiently. When it is used by insolvency practitioners, it furthers the public interest in regulating corporate activities.

Enabling law to be enforced supports the rule of law. It does so by removing the divide between declared law and practice, and ensuring that the law applies equally to all.

This is related to the consequences of the expansion of the state. It is nonsensical for the state to create rights, if those rights cannot be enforced and enjoyed. Similarly, it is nonsensical for the state to identify conduct as wrongful, but to enable wrongdoers to escape sanction with impunity, because the party affected by the conduct has no means.

Secondly, by enabling litigation to be commenced in circumstances where it might otherwise be financially impossible, litigation funding furthers the broader purpose of enabling the rights of individuals to be vindicated. It leads to the result that insufficiency of means will not arbitrarily deprive a claimant of the opportunity to be vindicated. It therefore serves a third purpose, of promoting equality between disputants.

Conclusion

This chapter has suggested that there is no problem of principle with a third-party controlling litigation. I have suggested that concerns about third-party control are best understood in the context of the traditional view of the civil justice system: a view which regarded party control as a central and important feature of the system. Concerns about third-party control have always been difficult to sustain, but modern

developments have made them untenable. In particular, the modern civil justice system has evolved to prioritise other values, for example through an increased emphasis on rights, the introduction of managerial values through the CPR, and the introduction of market forces to the legal profession. These changes to the civil justice system are reflective of broader changes in social values. Consequently, insofar as litigation funding has a tendency to lead to third party control of litigation, it is consistent with other trends in modern civil justice.

CHAPTER 5: DOES LITIGATION FUNDING COMMODIFY JUSTICE?

Introduction

The final criticism made of litigation funding is that it commodifies justice in some way – that is, it introduces market forces and market values into the civil justice system in a manner which is undesirable. This criticism is the subject of this chapter. I refer to this as the ‘commodification objection’.

What is wrong with commodification?

The first task is to identify what is meant by commodification. At its most narrow, it means that a good may be bought, sold and traded in a market. But this brings with it other aspects of market practice – in particular, what Radin describes as¹

market rhetoric, the practice of thinking about interactions as if they were sale transactions, and market methodology, the use of monetary cost-benefit analysis to judge these interactions.

Specific practices which are characteristic of markets include ‘supply and demand pricing, brokerage and arbitrage, advertising and marketing, stockpiling, speculation, and valuation in terms of the opportunity cost of production’.²

An accessible starting point for thinking about commodification is the work of Michael Sandel.³ Sandel distinguishes between unfairness in how a market operates, and problems caused by the mere existence of a market. As to the former, Sandel defined *coercion* as ‘the injustice that can arise when people buy and sell things under

¹ Margaret Jane Radin, ‘Market Inalienability’ (1987) 100 Harvard Law Review 1849, 1859; see also 1861.

² *ibid* 1855.

³ Michael Sandel, *What Money Can't Buy: The Moral Limits of Markets* (Allen Lane 2012).

conditions of severe inequality or dire economic necessity'.⁴ Thus, coercion is not an objection to a market per se, but rather to markets which operate in particular conditions – namely 'inequality severe enough to create coercive bargaining conditions'.⁵

Conversely, Sandel defined *corruption* as 'the degrading effect of market valuation and exchange on certain goods and practices'.⁶ In other words, the mere existence of a market may be objectionable, because 'Putting a price on the good things in life can corrupt them.'⁷ Further, markets create *inequality* – the disparities in wealth between rich and poor are more significant if more things are for sale in the market.⁸ The idea of a market in university places, for example, is offensive both because it reinforces *inequality*, and because it entails *corruption* of the virtues of a university, which ought to include the recognition of merit and the pursuit of excellence.⁹

Sandel observed that arguments against commodification have a common feature:¹⁰

To object that market valuation and exchange of a good corrupts its character is to assume that certain things are properly regarded and treated in certain ways.

Thus, a 'qualitative' judgment about the appropriate way to value an object is required in order to determine whether market valuation is appropriate or corrupting.¹¹

⁴ Michael J Sandel, 'What Money Can't Buy: The Moral Limits of Markets' (The Tanner Lectures on Human Values, Oxford, 11 and 12 May 1990), 94.

⁵ *ibid* 94-5.

⁶ *ibid* 94.

⁷ Sandel, *What Money Can't Buy: The Moral Limits of Markets* (n 3) 9.

⁸ *ibid* 8.

⁹ *ibid* 109-10.

¹⁰ Sandel 'What Money Can't Buy: The Moral Limits of Markets' (n 4) 101.

¹¹ *ibid* 101.

In a world of competing moral views, why not allow the market to decide? In other words, why not permit individuals to choose whether to participate in the market, and if they do, to choose the value they place on particular goods?¹² Radin suggests that adopting market rhetoric in relation to a good changes how society values that good.¹³ Thus, permitting any commodification of a good has a ‘domino effect’ on how society values all such goods.¹⁴

In the remainder of this chapter, I will use these concepts to analyse whether litigation funding is objectionable. In particular, I will consider the tendency (or otherwise) of litigation funding to create or reinforce *inequality*, and its tendency (or otherwise) to create or reinforce *corruption* of some value or good. Clearly, identifying the relevant value or good is critical.

What is the commodification objection to litigation funding?

Using this framework, we can consider the suggestion that litigation funding entails commodification of the civil justice system and/or the legal profession.

It was observed in Chapter 2 that one of the public policy concerns which drove maintenance and champerty was a concern to avoid ‘trafficking’ in litigation. In the case law, trafficking in litigation continues to be regarded as ‘objectionable’, although it is difficult to define. For example, the Court of Appeal has said:¹⁵

Trafficking in litigation is, by the very use of the word “trafficking”, something which is objectionable and may amount to or contribute to an abuse of the process. We think that it is undesirable to try to define in different words what would constitute trafficking in litigation. It seems to us to connote unjustified buying and selling of rights to litigation

¹² *ibid*; Radin (n 1) 1909.

¹³ Radin (n 1) 1877-87.

¹⁴ *ibid* 1912-13.

¹⁵ *Stocznia Gdanska SA v Latreefers Inc* [2001] 2 BCLC 116 (CA), [61].

where the purchaser has **no proper reason to be concerned with the litigation.**

It is common to find statements to the effect that ‘public policy frowns upon “trafficking in litigation”’.¹⁶ But this is a circular proposition: as the Privy Council has observed,¹⁷

“trafficking” is a pejorative term which takes the debate no further: it simply means trading in something (be it drugs or people) in which it is not permissible to trade.

In some cases, a profit motive is seen as a matter which has a tendency to increase the risk of abuse of process by the funder.¹⁸ Even where the court has endorsed litigation funding, the concept of trafficking is used as indicating where the permissible bounds might lie:¹⁹

... the courts must remain vigilant to ensure in the interests of public policy that there is no trafficking in litigation or speculating in causes of action for improper gain.

At the level of principle, excessive profit is a matter which can indicate champerty. But the hostility to profit-making in the conduct of litigation is more widespread. For example, as we will see, the profit motive of the funder is treated by Australian courts as a factor weighing in favor of ordering security for costs against a

¹⁶ *UTSA Pty Ltd (in liq) v Ultra Tune Australia Pty Ltd* (1996) 21 ACSR 457 (CA(Vic)), 463.

¹⁷ *Massai Aviation Services v Attorney General (The Bahamas)* [2007] UKPC 12, [19].

¹⁸ See, eg, *Factortame Ltd v Secretary of State for Transport, Local Government and the Regions (No 8)* [2002] EWCA Civ 932; [2003] QB 381, [84]-[85]; *Clairs Keeley (A Firm) v Treacy and Others* [2004] WASCA 277; (2004) 29 WAR 479, [125], [132]. The prospect of a funder abusing the process of the court was addressed separately in Chapter 3.

¹⁹ *Elfic v Macks* [2001] QCA 219; [2003] 2 Qd R 125, [65]. See also *Roux v Australian Broadcasting Commission* [1992] 2 VR 577, 606; *Faryab v Smyth* (CA, 28 August 1998); *Taylor v Hobson* [2016] QSC 226, [29].

funded claimant.²⁰ Commencing proceedings for the purpose of generating solicitors' fees is an abuse of process.²¹

Academic literature, too – even that which endorses litigation funding – shows a peculiar aversion to profit, such as reference to a funder's return as a 'windfall'.²² Concerns about the commodification of claims are often stridently expressed, but not explained.²³

Sometimes, there is concern about the introduction of market forces to the legal profession, or to the civil justice system. In Australia, Chief Justice Gleeson²⁴ treated litigation funding as essentially a regrettable necessity when he said that:²⁵

Litigation funding is now with us. It is not in all respects attractive, but subject to certain controls it may be a necessity. There is a need for some pragmatism about this, because the cost of access to justice is essentially a practical matter. Yet, a basic problem of access to civil justice is the remorseless mercantalisation of legal practice. This reflects the dominance of the culture of the market, with its tendency to reduce society to the single dimension of producers and consumers.

Keane JA²⁶ (writing extra-judicially) has gone further in deprecating the introduction of market forces to the legal profession via the medium of litigation funding. In a speech to the Judicial Conference of Australia concerning the harms of

²⁰ *Turner v Tesa Mining (NSW) Pty Limited* [2019] FCA 1644, [41], [71]-[72], [77].

²¹ *Treasury Wine Estates Ltd v Melbourne City Investments Pty Ltd* [2014] VSCA 351; (2014) 45 VR 585, [11]-[14].

²² See, eg, Poonam Puri, 'Profitable Justice: Aligning Third-Party Financing of Litigation with the Normative Functions of the Canadian Judicial System' (2014) 55 Canadian Business Law Journal 34, 37.

²³ See, eg, Andrew Cheng, 'Assignment of Bare Rights to Litigate: Assessing the Modern Doctrinal Position', 36.

²⁴ Gleeson CJ was one of the judges of the High Court of Australia in the majority in *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* [2006] HCA 41; (2006) 229 CLR 386.

²⁵ Chief Justice Murray Gleeson, 'Some Legal Scenery' (Judicial Conference of Australia, Sydney, 5 October 2007), 8-9.

²⁶ As he then was; his Honour was later elevated to the High Court of Australia.

litigation funding,²⁷ his Honour asserted that courts were ‘an arm of government charged with the quelling of controversies’. Consequently, litigants who used the court were ‘being governed’, and ought not to be regarded as ‘consumers of legal services’. His Honour emphasised that lawyers were officers of those courts – ‘they are not, and should not be thought to be, trading in legal services’. Instead, they are ‘participating in that aspect of government which establishes, in the most concrete way, the law of the land for the parties and for the rest of the community’. From this, his Honour concluded that the ‘exercise of judicial power’ should not be treated as commodity, and lawyers, as officers of the court, should not be engaged in any trade.

Clearly, litigation funding introduces or increases the prevalence of market forces in the civil justice system. It subjects causes of action to valuation and exchange, to market rhetoric, and treats them as a source of profit (to the funder) rather than compensation of the claimant, or law enforcement. The question is whether this is undesirable.

There are two aspects of the commodification objection. First, there is concern at the idea of causes of action being bought or sold, and the prospect of a market in legal claims. Secondly, there is concern at the prospect of the legal profession being subject to market forces. The remainder of this chapter deals with each aspect in turn.

²⁷ P A Keane, ‘Access to Justice and other Shibboleths’ (JCA Colloquium, Melbourne, 10 October 2009), 2.

Commodification of causes of action?

Wendel's work on commodification

The most developed account of the commodification objection is provided by Wendel,²⁸ who focuses his analysis on commodification of the cause of action.

Wendel notes (correctly) that the anti-commodification argument against litigation funding is rarely explained in detail. Wendel therefore seeks to develop the strongest anti-commodification argument against funding, and then to rebut it.

Wendel identifies that the gravamen of the anti-commodification argument is that litigation is intrinsically valuable – that is, inherently valuable in its own right – but ‘risks being corrupted by practices that treat it as instrumentally valuable’²⁹ – that is, as something which has value only because it can be exchanged for other things. Wendel argues that the strongest form of anti-commodification argument is ‘that the goal of profiting from an investment in a lawsuit is not a reason that should be taken in favor of participating in the civil litigation process’.³⁰ Thus, litigation investment ‘expresses an inappropriate attitude... towards the substantive value of civil justice’.³¹

In other words, the strongest anti-commodification argument against litigation funding proceeds as follows: litigation funding corrupts the civil justice system because it means people are participating for the wrong reason – profit – not the right reasons – seeking or providing a remedy. Thus, litigation funding demonstrates an inappropriate attitude towards ‘the underlying claim for civil justice’.

²⁸ W Bradley Wendel, ‘Alternative Litigation Finance and Anti-Commodification Norms’ (2014) 63 DePaul Law Review 655.

²⁹ *ibid* 665-6.

³⁰ *ibid* 686.

³¹ *ibid*.

However, Wendel observes that those who present the commodification objection often fail to identify properly what the *value* of litigation is; or, to put it another way, what is the *value* that is degraded or corrupted by the introduction of market forces.³² Wendel suggests that the strongest argument against commodification would focus on the concept of *corrective justice* – that there is something special about the relationship of claimant and defendant which requires that the rectification of loss be sought and provided between *them*, such that it would be inappropriate for a third party to intervene.³³

It may be accepted that corrective justice poses a challenge to funding, as Wendel identifies. In the following section, I draw upon corrective justice literature (already referred to in Chapter 3) to explain the full extent of the challenge.³⁴

Corrective justice theory and litigation funding

Corrective justice as a school of thought seeks to justify some part of private law³⁵ by reference to ‘the normative relationship between the parties’.³⁶ Thus, although there are a variety of corrective justice theories, the core idea is that of ‘correlativity’. As Weinrib explains:³⁷

Under this idea, liability reflects the conclusion that the defendant and the plaintiff have respectively done and suffered the same injustice. Correlativity structures this injustice: the elements of liability can be

³² *ibid.*

³³ *ibid* 691.

³⁴ I adopt Wendel’s starting point – i.e. that the strongest anti-commodification argument rests on theories of corrective justice. However, my analysis of corrective justice, and my response to the challenge, differs from that of Wendel.

³⁵ See William Lucy, *Philosophy of Private Law* (Oxford University Press 2007), 269 as to the applicability of particular theories of corrective justice beyond tort.

³⁶ Ernest J Weinrib, *Corrective Justice* (Oxford University Press 2012), 9.

³⁷ *ibid* 10.

explicated only in terms of concepts whose normative force applies simultaneously to both parties.

Weinrib's account, corrective justice is a 'structural principle', 'built into the very structure of liability as a normative phenomenon directly linking claimant and defendant'.³⁸ The claimant's injury, and the defendant's making good that injury, are two sides of the same coin: 'The defendant cannot be thought of as liable without reference to a claimant in whose favor such liability runs.'³⁹ This view is agent-relative – the identity of the claimant and defendant as victim and wrongdoer is important.

Wendel argues that it is not possible to oppose litigation investment on these grounds whilst simultaneously tolerating practices such as insurance and settlement.⁴⁰ What, then, does corrective justice have to say about insurance and settlement? There are differences of opinion amongst corrective justice theorists about whether insurance fits within the theory of corrective justice. But some corrective justice theorists do, indeed, contend that insurance does not fit into corrective justice theory.

For example, Weinrib regards the claimant-defendant relationship as so critical to the concept of corrective justice that insurance would run contrary to the concept.⁴¹ Weinrib directly refutes the suggestion that corrective justice permits the claimant to assign their claim, or to be compensated by a person other than the defendant.⁴² Rather:⁴³

³⁸ *ibid.*

³⁹ *ibid* 18, see generally 15-21 as to correlativity.

⁴⁰ Wendel (n 28) 691-4.

⁴¹ Weinrib (n 36) chapter 1, especially 14-15, 35-7; see also Richard W Wright, 'Substantive Corrective Justice Symposium: Corrective Justice and Formalism: The Care One Owes One's Neighbors' (1992) 77 *Iowa Law Review* 625, 703 (footnote 360) who reaches this conclusion after a survey of Weinrib's earlier work.

⁴² Weinrib (n 36) 88-92.

⁴³ *ibid* 87-8.

If the law took money from the defendant without giving it to the plaintiff, the injustice suffered by the plaintiff would remain uncorrected. Similarly, if the law gave money to the plaintiff without taking it from the defendant, the injustice done by the defendant would remain uncorrected. And even if the law took money from the defendant and gave an equivalent amount of money to the plaintiff in separate operations (say, by requiring payment into one government fund and out of another), the injustice as something done by the defendant to the plaintiff—and therefore as being of relational significance between them—would still remain uncorrected.

Unlike Weinrib, MacCormick does not consider that corrective justice requires a restoration of the position as between claimant and defendant. Instead, he refers to the need for reparation to be made to the victim when a right is infringed.⁴⁴ Thus, the obligation of reparation arises because:⁴⁵

individuals have as a matter of principle a right to reasonable security in their persons and possessions, and accordingly a right to be compensated when that reasonable security is infringed.

MacCormick considers that it is entirely permissible for the defendant to discharge their obligation of reparation by insurance.⁴⁶ Indeed, MacCormick goes on to suggest that there is a duty to insure when one engages in activities which will risk harm to others, to ensure that the obligation of reparation will be met.⁴⁷ MacCormick regards this obligation of reparation as having a corrective basis.⁴⁸ But there is no suggestion that corrective justice might accommodate a victim receiving less than full reparation.

⁴⁴ Neil MacCormick, *Legal Right and Social Democracy: Essays in Legal and Political Philosophy* (Clarendon Press 1982), 213, 217.

⁴⁵ *ibid* 214.

⁴⁶ *ibid* 217.

⁴⁷ *ibid* 218-19.

⁴⁸ *ibid* 226.

In a similar vein, Wright asserts that the concept of corrective justice, properly understood, does not require that the wrongdoer make good the obligation of compensation.⁴⁹ But Wright, too, places importance on the victim's loss being compensated fully.⁵⁰

It must be emphasised that these legal theorists all require that the *claimant* be compensated in full for their injury. Thus, whilst some accommodate an insurer sharing the *defendant's* burden in their corrective justice theories, they do not purport to accommodate the position of a third party sharing the *claimant's* recovery, or the claimant receiving less than full compensation.

Two things are critical for present purposes. First, corrective justice theories are agent-relative; that is, it matters that the claimant is the victim, and the defendant is the wrongdoer. Secondly, although there are some corrective justice theorists who can countenance a third party entering this equation, this debate occurs entirely on the defendant side – for example, considering whether insurers can be accommodated in a theory of corrective justice. Corrective justice theories do not purport to accommodate the concept of a third party sharing the claimant's recovery.

In fact, agent-relativity is a feature of much private law theory, not just corrective justice theory. Numerous examples can be found in the law and economics

⁴⁹ Wright (n 41) 703, citing only MacCormick (n 44) 217.

⁵⁰ Wright (n 41) 702-4, 706.

literature,⁵¹ and in rights-based accounts of private law,⁵² and in accounts of what unites private law,⁵³ about the importance to private law of the victim being the claimant, and being made whole by judgment.

⁵¹ A leading exponent of the law and economics school is Richard Posner, who argues that the purpose of damages in tort is ‘to deter uneconomical accidents’: Richard A Posner, *Economic Analysis of Law* (2nd edn, Little, Brown and Company 1977), 143.

Posner argued that because of this purpose of deterrence, the payment of damages *by the defendant* was ‘essential’: 143.

However, ‘that the damages are paid *to the plaintiff* is, from an economic standpoint, a detail’: 143. A footnote, however, notes that it is an ‘important’ detail: 143-4 (footnote 2). Enforcement by the claimant is important in economic terms because the claimant is most motivated to proceed against the defendant, and so the fact that a claimant brings an action promotes efficiency compared to the alternative of having the state investigate and prosecute private law: 400.

Enforcement by the claimant is also important, according to Posner, to deter the claimant from taking inefficient precautions against accidents: 143-4 (footnote 2).

The ninth edition of the text makes this point more emphatically and concisely; in dealing with ‘The Function of Tort Damages’, Posner’s introductory paragraph states:

Maintaining the credibility of the tort system requires that a defendant who is found liable must pay damages at least as great as L in the Hand Formula. And they must be paid to the victim rather than to the state as otherwise the victim will have no incentive to sue, and that incentive is essential to the maintenance of the tort system as an effective, credible deterrent to negligence. He may also take too many precautions.

Richard A Posner, *Economic Analysis of Law* (9th edn, Wolters Kluwer Law & Business 2014), 223.

⁵² For example, Robert Stevens argues that torts is most accurately thought of using a ‘rights model’: Robert Stevens, *Torts and Rights* (Oxford University Press 2007), 2-3. Critically for our purposes, it follows for Stevens that the identity of the claimant as victim is crucial:

The only person who can enforce a right is the right-holder, and persons who suffer loss because of the infringement of someone else’s right do not have standing to sue.

(at 173). Whilst Stevens considers several exceptions to this position, (at 174-98) none of the exceptions addresses (or is analogous to) the situation in which an assignee or third party funder enforces a right or shares the compensation.

⁵³ For example, Lucy seeks to identify the ‘structural’ features which unite private law, and distinguish it from public law. He defines private law’s structures to be the matters which

unify or underpin the evidential, procedural and doctrinal rules that give the private law relation its traditional form, namely, that of a dispute between two particular parties only, claimant and defendant.

Lucy (n 35) 22.

Lucy includes amongst these the fact that the remedy ordinarily takes the form of compensation, which must be provided by the defendant, and arises from the fact of a past wrongdoing. Thus, ‘private law binds claimants and defendants together through the medium of compensation’ and ‘only through the nexus of one having allegedly wronged the other’ (see 23). Lucy claims that it is these features which have led some proponents of corrective justice theory to describe private law as ‘bilateral’ (see 24, citing Coleman and Weinrib).

In summary, we can see that litigation funding is objectionable from a corrective justice standpoint. Wendel responds to this challenge by claiming that insurance and settlement are relevantly similar to funding, and that, therefore, one cannot tolerate the former and also oppose funding. But this is an unsatisfactory argument – some corrective justice theorists do, indeed, regard insurance and settlement as inconsistent with the theory.

Commodifying causes of action: an alternative analysis

Nevertheless, the suggestion that litigation funding is objectionable because it entails commodification of causes of action ought to be rejected – albeit for different reasons to those proposed by Wendel.

Turning first to the question of *inequality*, there might be valid concerns about the risk of unfairness of the litigation funding market. This topic is explored further in Chapter 8. However, this is a potential inequality in the manner in which the market operates. It is not an inequality which arises through the very existence of a market.

In the absence of litigation funding (or some other assignment of a cause of action), there is a market for causes of action. However, it is a highly limited and inefficient market – a monopsony, in economic terms – because there is only one potential purchaser of a cause of action: the defendant (who, may, in effect, choose to purchase the cause of action through settlement). If there is only one potential purchaser for a claim (i.e. the defendant, via settlement), it can rationally be expected that its price will be lower than if there were a larger market.

In fact, if an impecunious claimant has a cause of action, but cannot assign it or seek third party funding (whether in the form of legal aid, litigation funding, or otherwise), then their claim may be virtually worthless. Such a claimant will not be

able to pursue their claim to judgment, and there will therefore be little incentive for the defendant to offer any settlement. Conversely, a wealthy claimant is not constrained in this way: they can litigate to judgment if they choose, and their ability to do so means they are in a stronger bargaining position to seek a settlement.

If a market for causes of action exists (in the form of assignment, or third-party funding), then the claimant has a valuable asset, which it can sell to the highest bidder. Sandel argued that disparities in wealth are worse if more things are for sale. But this is because the lack of purchasing power of the poor is made more acute if they are required to apply their resources to a wider range of goods. Creating a market for causes of action may well *reduce* inequality for the impecunious claimant, by giving them the same power in litigation as the wealthy claimant.

We can then turn to the separate, and more difficult, question of corruption. We can accept Wendel's analysis that insofar as litigation funding might *corrupt* some value, it is most likely to corrupt values arising from theories of corrective justice. In other words, if corrective justice requires that the wrongdoer (and no-one else) compensates the victim (and no-one else), then third-party litigation funding is inconsistent with this.

The relevant value, or good, would be the moral requirement that a claimant be fully restored to the status quo ante (as far as a court remedy can achieve that), and that the defendant ought to make reparation. From a commodification point of view, the objection would be that litigation funding corrupts this value, because funders are engaged in litigation for profit, and not to achieve this moral requirement, and also because, by sharing in the claimant's recovery, the claimant cannot be restored to the status quo ante.

Three responses can be made to this. First, the criticism may be deflected by pointing to a more important value of the civil justice system: the rule of law. In Chapter 3, I considered the importance of the rule of law, and explained that one aspect of the rule of law is to ensure that the law is actually enforced. This is the pre-eminent value of the civil justice system; without enforcement of law, no other value (such as those arising from corrective justice) can be served. In Chapter 3, I explained that litigation funding served to further the rule of law.

Secondly, litigation funding is a solution to the problem of high and unpredictable legal costs; a problem which, in itself, provides a challenge to corrective justice, as it deters claimants from seeking the mutual restoration and reparation that a judgment offers. Litigation funding may be difficult to accommodate in a corrective justice theory, but in a non-ideal world, it must be more attractive than the alternative, which is for wrongs to go unremedied because the claimant lacks the funds or the appetite for litigation.

Thirdly, the fact that litigation funding does not fit into corrective justice theory is more problematic for the theory than the practice of funding. All of the accounts of corrective justice which have been set out earlier in the chapter seek to theorise private law from an *internal* point of view.⁵⁴ These theorists therefore seek to provide an account of private law which is consistent with the law's own internally-determined reasons. Thus, it is not only appropriate but *necessary* to assess these theories of law against the self-understanding of those who create, develop and enforce private law (judges and legislators), because that is the methodological approach that those theorists

⁵⁴ Lucy (n 35) 41; Weinrib (n 36) 10-11.

have adopted.⁵⁵ Insofar as accounts of private law seek to provide an accurate description, there is a threshold level of ‘fit’ that must be met. It would be impossible for any account of private law to accommodate every judgment, statute, and feature of practice – not least because law itself contains exceptions and anomalies.⁵⁶ However, if a theory of private law fails to accommodate significant features of private law, then it has failed in its descriptive endeavour.⁵⁷

There are many practices in the modern civil justice system which challenge the values of corrective justice. As explained earlier, some theories of corrective justice do *not* accommodate insurance. Practices which undermine the law’s capacity to restore the claimant to the status quo ante – something which all corrective justice theorists seem to regard as essential – are the use of contingency fees, assignments of debts, subrogation of claims by insurers, the assignment of the fruits of litigation (which was always permissible), settlement of a claim for less than the quantum of the claimant’s loss, and the imposition of costs on a successful claimant (for example, because of a difference between the solicitor-client costs and the party-party costs).

Further, there are many areas of substantive law which do not fit within the ambit of corrective justice. Obvious examples include vicarious liability – in which a person other than the wrongdoer provides compensation (such as an employer compensating a victim for the tort of their employee) – and the imposition of gain-

⁵⁵ Lucy (n 35) 272 (citing Hart and Dworkin), 273 (explaining how the corrective justice accounts of Coleman and Weinrib adopt this methodological approach).

⁵⁶ For example, legislation does not have to achieve philosophical consistency in the same way that judgments must in a system of stare decisis; there are anomalous rules and exceptions in the substantive principles of law; disparate areas of law may evolve in a diverging manner; judges make mistakes.

⁵⁷ Cf Lucy (n 35) 276-83.

stripping remedies, where the compensation to the claimant bears no relationship to their loss.

One reason why all of these practices might be permitted is because the moral value of corrective justice is outweighed by competing values: specifically, the need to ensure that litigation and law enforcement are not contingent on the claimant's capacity or appetite for litigation, and/or the interest in enabling the claimant to arrange their affairs as they choose, and/or the need to enforce the law and thus provide sufficient deterrence to defendants.

Conclusion

I started this section by explaining that there are two wrongs of commodification: creating inequality, and corrupting some value inherent in the subject. This first section has focused on the potential for litigation funding to commodify, undesirably, causes of action.

The strongest argument against the commodification of causes of action is that it entails an inappropriate attitude towards the value of the claim, which is grounded in corrective justice. Corrective justice, however, does not provide a good ground for concern about the commodification of causes of action.

In the second part of this chapter, I turn to the suggestion that litigation funding undesirably commodifies the legal profession.

Commodification of the civil justice system or the legal profession?

The second aspect of the commodification objection is the suggestion that litigation funding entails an undesirable commodification of the legal profession.

A reminder is necessary about the meaning of commodification.⁵⁸ Legal services have always been commodified in a narrow sense – available to be bought and sold in a marketplace. But, until recently, the market for legal services lacked important features of a market. First, there were rules and practices – such as the prohibition on advertising – that restricted the operation of market forces. Secondly, the profession eschewed market values, or ‘market rhetoric’,⁵⁹ in how it viewed itself, and projected itself to the rest of society.

A profession and not a trade: a history of rejecting market values

One feature or value of the legal profession which was expressly recognised in England and Australia by the late nineteenth century – and which was latent in professional practice prior to that – was the idea that law was a profession and not a ‘mere money-making trade’. Larson has suggested that an adherence to anti-market sentiment, in the face of society’s move towards capitalism in the nineteenth century, was how the professions sought to distinguish themselves from trades.⁶⁰ The distinguishing characteristics of a professions have been said to be that:⁶¹

First, work is valued for its intrinsic reward, rather than for the income it provides, and is seen as a calling or vocation. Second, is the idea that services are universally available, which reflects the notion of community responsibility and gentlemanly disinterest. Third, the aristocratic idea that rank carries responsibilities, or *noblesse oblige*.

⁵⁸ See the discussion above at the text accompanying footnotes 1 and 2.

⁵⁹ This is the term used by Radin, explained in the quote accompanying footnote 1 above.

⁶⁰ Magali Sarfatti Larson, *The Rise of Professionalism: Monopolies of Competence and Sheltered Markets* (2nd edn, Transaction Publishers 2013).

⁶¹ Andrew Boon, *The Ethics and Conduct of Lawyers in England and Wales* (3rd edn, Hart Publishing 2014), 54-5, citing Larson (n 60) 13, 62.

In the context of the legal profession, Roscoe Pound's account of the elements of professionalism is often cited. He identified three aspects to professionalism:⁶²

Historically there are three ideas involved in a profession: organization, learning, i.e. pursuit of a learned art, and a spirit of public service. These are essential. A further idea, that of gaining a livelihood is involved in all callings. It is the main if not the only purpose in the purely money-making callings. In a profession it is incidental.

The centrality of public service, and of money-making being incidental, was made stark in Pound's elaboration of the three elements:⁶³

In the third idea, however, we have the point of chief importance. It is of the essence of a profession that it is practiced in a spirit of public service. ... The best service of the professional man is often rendered for no equivalent or for a trifling equivalent and it is his pride to do what he does in a way worthy of his profession even if done with no expectation of reward. This spirit of public service in which the profession of law is and ought to be exercised is a prerequisite of sound administration of justice according to law. The other two elements of a profession, namely, organization and pursuit of a learned art have their justification in that they secure and maintain that spirit.

Thus, for Pound, the 'spirit of public service' – and with it the rejection of market values – underpinned the other two elements of professionalism. It was also said to be necessary for the proper administration of justice.

The hostility to market values manifested itself in a variety of specific rules of conduct or ethics. For example, in both jurisdictions, lawyers were either prohibited from advertising, or discouraged from doing so. Lawyers were not permitted to split their fee with non-lawyers. These rules were enforced at different times by either the exercise of the self-regulatory powers of the profession, or the social pressure which existed at a time when the profession was relatively small and homogenous.

⁶² Roscoe Pound, *The Lawyer from Antiquity to Modern Times* (West Publishing 1953), 6.

⁶³ *ibid* 9-10, see also 4-6.

In this section, I will consider first how these sentiments and rules developed. I will start by considering the approach taken in the United States in the early twentieth century to the regulation of the legal profession: express written codes of ethics were adopted there earlier than in England, but reflected what was understood to be the English position concerning legal professional ethics. The regulation of the American legal profession therefore sheds light on the state of the English legal profession at a time when the English profession had not yet engaged in similar self-reflection. I then consider the position in England.

United States

In 1908, the American Bar Association promulgated a code of ethics, which was not replaced until 1970. In the mid to late nineteenth century, the American legal profession had suffered a diminution in its prestige;⁶⁴ this followed what Roscoe Pound described as an ‘era of decadence’ in the profession.⁶⁵

There were many public statements from the time concerning declining moral standards in the profession, and attributing this to a failure to appreciate the significance of a law being a profession and not a trade,⁶⁶ including well-publicised speeches made by President Roosevelt and Louis Brandeis (later a Supreme Court Justice).⁶⁷ Spurred by the criticism that the legal profession had succumbed to commercial values, the American Bar Association sought to reinvigorate the sense of moral virtue of the

⁶⁴ Russell G Pearce, ‘Lawyers as America's Governing Class: The Formation and Dissolution of the Original understanding of the American Lawyer's Role’ (2001) 8 University of Chicago Law School Roundtable 381, 395-6.

⁶⁵ It should be noted that the idea of the lawyer as the disinterested professional serving the public interest rather than their own interest had earlier origins in the republican tradition: see generally *ibid* 386-7.

⁶⁶ *ibid* 396 (and the references there cited).

⁶⁷ James M Altman, ‘Considering the ABA's 1908 Canons of Ethics’ (2003) 71 Fordham Law Review 2395, 2403-9.

profession. In a 1906 report, the ABA committee identified that the vice to which the new code would be directed was an observation that⁶⁸

... the trend of many is away from the ideals of the past and the tendency more and more to reduce our high calling to the level of a trade, to a mere means of livelihood or of personal aggrandizement.

Specifically, the committee singled out for criticism of those who treated the law as a business. Such lawyers were referred to as ‘the shyster, the barratrously inclined, the ambulance chaser, the member of the Bar with a system of runners’, and were ‘controlled by graft, greed and gain, or other unworthy motive.’⁶⁹ These lawyers were said to ‘lower the *morale*’ of the legal profession, and to ‘debase our high calling in the eyes of the public’.⁷⁰

At around this time, the ABA also republished an influential essay by Sharswood.⁷¹ Considering the circumstances of the Roman legal profession, and the English bar, Sharswood made clear that the elite members of those professions had made a virtue of eschewing commercial values.⁷² He noted the pragmatic retort that lawyers were no less entitled than any other worker to be paid, but considered such arguments ‘more plausible than sound’; rather, public interest required a ‘high-minded, honorable Bar’, whereas ‘custom-seeking, money-making lawyers [were] one of the

⁶⁸ American Bar Association Committee on Code of Professional Ethics, ‘Report’ (1906) 29 Annual Report of the American Bar Association 600, 601.

⁶⁹ *ibid.*

⁷⁰ *ibid* 602.

⁷¹ George Sharswood, ‘Professional Ethics’ (1907) 32 Reports of the American Bar Association 9. The essay was a later edition of a speech which had originally been delivered in 1854. See also Pearce (n 64).

⁷² Altman (n 67) footnote 426. For example, having documented the history of the Roman legal profession, noting its origins as a gratuitous service, and decline into various abuses, asking rhetorically ‘Is not this probably the history of the decline of the profession in all countries from an honourable office to a money-making trade?’: Sharswood (n 71) 136-42, especially 142. Sharswood considered too the position of the English profession, and noted that the rule against suing clients for fees was unique to the bar; contrasting that with the practice of ‘mere attorneys’: 142-4.

greatest curses with which any state or community can be visited'.⁷³ Sharswood, though, envisaged that no 'poor man with an honest cause' would be without a lawyer; rather, it would be the 'duty, perhaps more properly his privilege, to work for nothing'.⁷⁴

Unsurprisingly, therefore, one of the important projects of the ABA code was to launch a counterattack on the forces of commercialisation.⁷⁵ It did this in part by setting out a series of normative statements about the purpose of the legal profession. Two were particularly important. First, there was the condemnation of advertising,⁷⁶ which was thought to lead to other vices.⁷⁷ As Altman explains:⁷⁸

... around the turn of the twentieth century, it was commonly believed that a lawyer who acted like a tradesman in getting a client – for example, by advertising his 'wares,' underbidding his competition, or exaggerating his experience or competence – would be less likely to act 'professionally' in representing that client.

Thus, referral fees were also treated as unprofessional, as was seeking to poach the clients of other lawyers.⁷⁹

Secondly, canon 12, which addressed the principles upon which fees should be set, concluded with the words

In fixing fees it should never be forgotten that the profession is a branch of the administration of justice and not a mere money-getting trade.

⁷³ Sharswood (n 71) 147-8.

⁷⁴ *ibid* 151.

⁷⁵ This is discussed at greater length by Altman (n 67) 2475-91.

⁷⁶ See generally American Bar Association, *Canons of Professional Ethics* (1908), canon 27.

⁷⁷ The prohibition against advertising was the introduction of a new norm (adopted from the English bar). American lawyers had previously advertised – including those such as Abraham Lincoln and David Hoffman who in other respects were seen as paradigms of the professional lawyer: Altman (n 67) 2484-7. See also Pearce (n 64) 413.

⁷⁸ Altman (n 67) 2484.

⁷⁹ American Bar Association, *Canons of Professional Ethics* (1908), canon 27; canon 7.

In a similar vein, the canons cautioned against disputes between lawyer and client concerning fees, and stated that lawsuits to recover fees were permissible only ‘to prevent injustice, imposition or fraud.’⁸⁰

Thus, in developing the code, the ABA drew on English principles of legal professional ethics – albeit, as will be seen, that those principles had not yet been codified in England.

England

The legal profession in England has only engaged in comprehensive self-regulation in relatively recent times. The first regulations devised by the Law Society were the Solicitors’ Practice Rules of 1936, a brief document which outlawed advertising, referral fees, arrangements to share fees with non-lawyers, and charging fees at a rate less than the scale.⁸¹ Guidelines for etiquette at the bar were first published in 1875, but did not take the form of a regulatory code.⁸²

Nevertheless, the English profession had rules of practice and etiquette that eschewed commercial values. Indeed, the ABA had drawn on these in drafting its own code. The rules of the bar were informal, and binding by virtue of social pressure only.⁸³ Indeed, the senior echelons of the bar were opposed to the creation of formal rules.⁸⁴

⁸⁰ *ibid*, canon 14.

⁸¹ Boon (n 61) 144.

⁸² *ibid* 147.

⁸³ William H Hurlburt, *The Self-Regulation of the Legal Profession in Canada and in England and Wales* (Law Society of Alberta; Alberta Law Reform Institute 2000), [216]-[221].

⁸⁴ *ibid* [217].

It is clear that the English profession adhered to the ideals identified by Pound⁸⁵ – public service, mastery of the discipline, and disinterest in profit-making – albeit that these were not stipulated in express conduct rules. Lord Macmillan expressed the position in the following terms:⁸⁶

We call ourselves a learned profession. Let me remind you that we are also a liberal profession. The difference between a trade and a profession is that the trader frankly carries on his business primarily for the sake of pecuniary profit while the members of a profession profess an art, their skill in which they no doubt place at the public service for remuneration, adequate or inadequate, but which is truly an end in itself. The professional man finds his highest rewards in his sense of his mastery of his subject, in the absorbing interest of the pursuit of knowledge for its own sake, and in the contribution which, by reason of his attainments, he can make to the promotion of the general welfare. It is only by the liberality of our learning that we can hope to merit the place in public estimation which we claim and to render to the public the services which they are entitled to expect from us.

These ideals originated centuries earlier. As early as the 1640s, the English bar had stated its commitment ‘to act in the public interest, to represent all comers, not to tout or enter into improper contracts with particular solicitors for the supply of business’.⁸⁷ Baker has observed that by around the 16th or 17th century,⁸⁸

... the Inns, encouraged by the judges, began to insist upon the gentility of their members, and to aspire to the neo-classical ideal of a profession of gentlemen, detached from the pursuit of lucre and united in their devotion to a superior vocation.

Accordingly, it was regarded as inappropriate for barristers to discuss fee arrangements with solicitors; this role was fulfilled by the barrister’s clerk.⁸⁹ This was

⁸⁵ See the quotes set out in the text accompanying footnotes 62 and 63 above.

⁸⁶ Hugh Pattison Macmillan, *Law & Other Things* (The University Press 1937), 127.

⁸⁷ Michael Burrage, *Revolution and the Making of the Contemporary Legal Profession: England, France and the United States* (Oxford University Press 2006), 398.

⁸⁸ Hurlburt (n 83) [307].

⁸⁹ Boon (n 61) 46.

still a matter of professional etiquette in the early twentieth century.⁹⁰ Barrister's fees were treated as honoraria only, a tradition originating in ancient Rome where the role of advocate was taken on only by the wealthy, and parties were required to swear that they had not paid or promised a fee to their advocate.⁹¹ Thus, a barrister was not able to sue in the event that their fees were unpaid.⁹² It was not until the *Courts and Legal Services Act* of 1990 that barristers were enabled to enter contracts for their fees.⁹³ Rules of professional conduct for both barristers and solicitors precluded the use of advertising.⁹⁴

The suggestion that profit-making is *incidental* to the legal profession, rather than its purpose, continues to have modern adherents in England. For example, Boon identifies as one of the four 'core values' of the legal profession the idea of 'public service'; the idea that a lawyer ought to be more interested in the public value of his work than in any 'extrinsic reward, money or prestige, it offers'.⁹⁵

The causes and consequences of rejecting market values

The rejection of market values was driven by the elite of the profession

It was not the case that the American legal profession was uniformly hostile to commercial values.⁹⁶ The hostility to commerciality – including specifically

⁹⁰ Frederick Cecil Gurney Gurney-Champion, *Justice and the Poor in England: An Account of the Position of the Poor in Legal Matters in England and Wales; and a Study of the Inequality in the Administration of Justice* (George Routledge & Sons Ltd 1926), 7.

⁹¹ Pound (n 62) 51-5; see 68, 104 as to the rule's English reception.

⁹² Boon (n 61) 416.

⁹³ Courts and Legal Services Act 1990 (UK), s 61.

⁹⁴ William Whytehead Boulton, *A Guide to Conduct and Etiquette at the Bar of England and Wales* (6th edn, Butterworths 1975), 55.

⁹⁵ Boon (n 61) 5-6.

⁹⁶ See, eg, Pearce (n 64) 393, 396.

contingency fees – was driven by the elite of the profession. Wealthy and established lawyers, who had wealthy and powerful clients, had little need to advertise, and their clients could afford to pay on an hourly basis.⁹⁷ In fact, the ABA itself was not at that time a representative body, but was ‘an exclusive social fraternal organization of high-status lawyers’, which sought to enhance the social standing of the profession.⁹⁸

As in the United States of the early twentieth century, the division of the English profession which was most opposed to commodification was the division which enjoyed the greater status and financial security: the bar. In England, however, the opposition to commodification had a much longer history.

Indeed, the stratification of the English legal profession into barristers and solicitors – which today is a distinction in function or role – was originally a division based on status.⁹⁹ The stratification of the profession led to the division in function, as those members of the legal profession who enjoyed a higher status came to reject more routine and mundane work, and came to accept briefs only from solicitors, and not directly from clients; these developments in function, in turn, came to ‘reinforce... [the] image of the common lawyer as disinterested and honourable counsellor’.¹⁰⁰ From these origins grew the greater ‘vocational autonomy’ of the bar; while solicitors were subject to more extensive external regulation, barristers were ‘generally more conscious

⁹⁷ Altman (n 67) 2490-1; cf Pearce (n 64) 396-7.

⁹⁸ Charles W Wolfram, ‘Toward a History of the Legalization of American Legal Ethics - I. Origins’ (2001) 8 University of Chicago Law School Roundtable 469, 485.

⁹⁹ Wilfrid R Prest, ‘Lawyers’ in Wilfrid R Prest (ed), *The Professions in Early Modern England* (Croom Helm 1987), 80-1; see also Wilfrid R. Prest, *The Rise of the Barristers: A Social History of the English Bar 1590-1640* (Paperback (with corrections) edn, Clarendon Press), 12. Burrage, *Revolution and the Making of the Contemporary Legal Profession: England, France and the United States* (n 87) 396, refers to an express statement of the Inns in 1614 that ‘attorneys and solicitors [were] but ministerial persons and of an inferior nature’. See also Boon (n 61) 57.

¹⁰⁰ Prest ‘Lawyers’ (n 99) 82-4, esp 84.

of being “by their profession... the first class of gentlemen” than anxious to assert and defend the social importance and worth of their calling’.¹⁰¹ The association of the bar with the upper classes was not accidental: the selection process, and the financial demands, served to limit admission to the profession to the wealthy.¹⁰² Indeed, one aspect of barristers’ etiquette was that they not engage socially with solicitors.¹⁰³

Solicitors came to gain the indicia of professionalism in the mid-nineteenth century, and largely followed the example of the bar in developing their own profession.¹⁰⁴ Like the ABA, the English Law Society initially drew its membership from the elite of the profession (namely, those who practised in London, in litigation).¹⁰⁵ Like the ABA, the English Law Society at times sought to impose the values of the elite on the lower echelons of the profession.¹⁰⁶ Admission to practice as either a barrister or a solicitor became meritocratic during the nineteenth century through the introduction of examinations.¹⁰⁷ However, in practice, the Law Society continued to be dominated by the partners of leading London solicitors’ firms, who were part of a social elite (and introduced their sons into the same social spheres);¹⁰⁸ prior to the Second World War, 75% of law students studied at Oxford, Cambridge, or

¹⁰¹ *ibid*, 85.

¹⁰² Hurlburt (n 83) [175]-[182]; Richard Abel, ‘The Decline of Professionalism?’ (1986) 49 *Modern Law Review* 1, 2-3. Becoming a solicitor also entailed significant expenses, but these were less onerous: Abel, 4.

¹⁰³ John H Baker, *The Legal Profession and the Common Law: Historical Essays* (Hambledon Press 1986), 118; Burrage, *Revolution and the Making of the Contemporary Legal Profession: England, France and the United States* (n 87) 527-8.

¹⁰⁴ Boon (n 61) 47-9.

¹⁰⁵ Hurlburt (n 83) [90]-[93]; *ibid* 48-9.

¹⁰⁶ See, eg, Boon (n 61) 63, who reports that ‘When provincial solicitors sought County Court rights of audience in the nineteenth century, the Council of the Law Society rejected the proposal because “gentlemen did not frequent the county court”.’

¹⁰⁷ *ibid* 52-3.

¹⁰⁸ *ibid* 53-4.

one of the three London law faculties.¹⁰⁹ The English legal profession only really became more socially diverse from the 1970s onwards.¹¹⁰

Economic analysis

Some economists and sociologists have suggested that the restrictive practices of the legal profession have served to further the economic interests of its members. On this view, professionalism is a means to secure control of the market; control can then be exerted in the profession's economic self-interest.¹¹¹ As Larson has explained:

Anti-market and anti-capitalist principles were incorporated in the professions' task of organizing for a market because they were elements which supported social credit and the public's belief in professional ethicality.¹¹²

On this model, Abel and Lewis are cynical about the sincerity of anti-market sentiments.¹¹³

Lawyers' self-exhortations – in ethical codes, bar association journals, and annual conventions – presumably are intended primarily for public consumption, or at least as a means of collective self-deception or reassurance. For social scientists to confuse those prescriptions with actual behaviour would display unparadigmatic naivete.

Some aspects of this view are consistent with how the legal profession came to self-regulate in England. As observed earlier, the rejection of market values was sometimes asserted to be necessary for the administration of justice. In England, the

¹⁰⁹ Abel 'The Decline of Professionalism?' (n 102) 10.

¹¹⁰ Boon (n 61) 65.

¹¹¹ Richard L Abel, *The Legal Profession in England and Wales* (Basil Blackwell 1988), 7-21, and see generally Chapters 2, 5, 10 and 12. See also Abel 'The Decline of Professionalism?' (n 102) 1, 15-20. Frank H Stephen, *Lawyers, Markets and Regulation* (Edward Elgar 2013), 12 describes this as a 'private interest' or 'capture' theory.

¹¹² Larson (n 60) 63.

¹¹³ Richard L Abel and Philip SC Lewis, 'Putting Law Back into the Sociology of Lawyers' in Richard L Abel and Philip SC Lewis (eds), *Lawyers in Society: Comparative Theories* (University of California Press 1989), 495. See also Hurlburt (n 83) [332]-[333].

profession was permitted to self-regulate until relatively recently because it successfully claimed to be ‘the primary custodians of the public interest on legal matters’.¹¹⁴ It could be argued, therefore, that eschewing market values was an aspect of the profession’s claim to represent the public interest, which in turn supported its claim to self-regulation.

It has been suggested that the bar’s efforts to distance itself from solicitors, not to take briefs directly from clients, and interposing clerks between barristers and solicitors, are difficult to justify in economic terms, in that they place control of barristers’ earnings in the hands of others – and that they are better-explained as a means of enhancing status.¹¹⁵ However, enhancing status may, itself, generate financial rewards – as we have observed above, these rules were driven by the most wealthy echelon of the profession, who worked for wealthy and powerful clients. Further, as Radin observes, those who oppose commodification¹¹⁶

might be primarily people whose wealth and power make them comfortable enough to be concerned about the inroads on the general quality of life that commodification would make.

How did the restrictive practices of lawyers affect clients? In the later parts of the twentieth century, economists came to express the view that the anti-market rules and practices of the legal profession were restrictive, and served to ‘inhibit competition in the market for legal services to the detriment of consumers of these services’.¹¹⁷ In relation to advertising, economists’ opposition to restrictions originated with the work

¹¹⁴ Michael Burrage, ‘From a Gentlemen's to a Public Profession: Status and Politics in the History of English Solicitors’ (1996) 3 *International Journal of the Legal Profession* 45, 64-6.

¹¹⁵ *ibid* 59; Burrage, *Revolution and the Making of the Contemporary Legal Profession: England, France and the United States* (n 87) 526-8.

¹¹⁶ Radin (n 1) 1917.

¹¹⁷ Stephen (n 111) 1.

of Stigler in 1961. Stigler argued that restricting advertising disadvantaged clients, because it reduced competition between lawyers, and increased the cost to the client of finding a lawyer. The empirical evidence supports the view that restricting advertising increased the price of legal services.¹¹⁸ However, when lawyers advertised their prices, this can be perceived by prospective clients as an indicator of poor quality.¹¹⁹

In a detailed review of the economic literature concerning the regulation of the legal profession, Stephen explains that there may be good economic reasons to regulate the profession, which are different to the ‘traditional’ reasons given by the profession (such as the need to protect the administration of justice).¹²⁰ From an economics perspective, the need to regulate the legal profession stems from the fact clients are at a disadvantage in selecting and supervising lawyers, which can be described as an ‘information asymmetry’: they have no way to identify a good lawyer before entering the retainer, and they are unlikely to be able to identify flaws in the service even after it has been provided.¹²¹ This leads to specific problems such as ‘adverse selection’, or a ‘market for lemons’, where quality is driven down because clients cannot identify and reward high quality, or the temptation for lawyers to over-service once they have been retained.¹²²

The anti-commodification rules did not, however, address these problems. For example, problems of information asymmetry are not dealt with by preventing direct access, or preventing advertising. So, even if we were to endorse self-regulation on economic grounds, the anti-commodification rhetoric and rules did no seem to address

¹¹⁸ ibid 99-100.

¹¹⁹ ibid 28; 98-100.

¹²⁰ See generally ibid chapter 2.

¹²¹ ibid 12-14.

¹²² ibid 12-16.

the market failures in the market for legal services. In any event, there is little *empirical* evidence about the effect of restrictions on the market for legal services.¹²³ Thus, it is unclear that anti-commodification practices and rhetoric of the legal profession had any positive effect on clients.

Did rejecting market values serve the interests of clients?

The rejection of market values did not lead to a commitment to access to justice for the poor. For example, the English Law Society was opposed to most proposals for expanding legal services for the poor in the period before World War Two.¹²⁴ Writing in 1926, Gurney-Champion observed that although there were many lawyers who provided free legal services to the poor, this was not a matter in which they would have taken professional pride. On the contrary, Gurney-Champion observed that ‘it is not yet thought a desirable thing or an honourable thing in professional circles to give the poor free legal advice. Without question a solicitor loses [sic] caste by doing so.’¹²⁵

By the early twentieth century, it was observed in England that (as in the United States) there was a lower echelon of the profession which worked on a no-win, no-fee basis. However, Gurney-Champion observed that such work was often conducted in a manner exploitative to the client, stating: ‘Probably the poor are victimized by nothing so much as by some of these speculative low-class solicitors.’¹²⁶

¹²³ *ibid* 1, 35, Chapter 6.

¹²⁴ Boon (n 61) 55.

¹²⁵ Gurney-Champion (n 90) 8; see also 17.

¹²⁶ *ibid* 8.

Summary

In the first part of the twentieth century, we can see that an important aspect of the legal profession's self-identity was that it was a profession, and not a 'mere money-making trade'. We can be sceptical about the sincerity of this sentiment, and also any suggestion that it benefited clients.

Nevertheless, the idea that profit-making by lawyers is unseemly has echoes in the modern legal profession. Criticism of third-party litigation funding which arises from the commodification of the legal profession must be understood in light of this long tradition.

However, as will be seen in the next section, important developments in the second half of the twentieth century have meant that commercial values are now firmly entrenched in the legal profession. As a consequence, the modern legal profession ought to be regarded as a market.

Concerns about the commodification of the legal profession are misplaced

The legal profession has been subject to a number of reforms which have had the effect of introducing market forces, particularly since the 1970s.¹²⁷ As noted earlier,¹²⁸ the legal profession has always had some elements of commodification – most obviously, services have always been bought and sold. However, it did not have all of the features of a market, because of restrictive rules and practices. The profession also sought to reject market rhetoric and market methodology in its self-assessment, and its self-regulation, and in how it presented itself to the rest of society.

¹²⁷ Joseph M Jacob, *Civil Litigation: Practice and Procedure in a Shifting Culture* (EMIS Professional Publishing 2001), 2, 9, 92-101.

¹²⁸ See the text accompanying footnote 58.

Several commentators have observed that the changes in the legal profession in the past 50 years have reflected broader changes in society. At a high level of abstraction, a significant social change since the 1970s has been the rise of consumerism, which in turn fosters a market in which there is competition.¹²⁹ Specifically, this has manifested itself in changes to the rules concerning advertising in the legal profession, changes to the competition of lawyers, and changes to lawyers' remuneration.

England

The 1960s and 1970s saw enormous changes in the legal profession. First, the profession greatly expanded, and became more socially diverse.¹³⁰ This, of itself, is likely to have enhanced competition,¹³¹ and one might expect that increased social diversity reduces the likelihood that members of the profession will share the same values.

Secondly, the limit on the number of partners in law firms (which had been set at 20) was legislatively abolished in 1967.¹³² Large law firms have therefore come to resemble other large businesses, with the commercial characteristics that entails.¹³³

The introduction of market forces into the legal profession accelerated during the 1980s, with the Thatcher government's commitment to increasing competition and opening markets.¹³⁴ Important developments in this period included removing lawyers'

¹²⁹ Jacob (n 127) 2, 9; see also Boon (n 61) 64.

¹³⁰ Boon (n 61) 67-8.

¹³¹ Burrage, 'From a Gentlemen's to a Public Profession: Status and Politics in the History of English Solicitors' (n 114) 75.

¹³² Companies Act 1967 (UK), s 120(1)(a).

¹³³ Boon (n 61) 69-70, 72, 116-18.

¹³⁴ Richard Abel, 'The Politics of Professionalism: The Transformation of English Lawyers at the End of the Twentieth Century' (1999) 2 Legal Ethics 131, 131; Hurlburt (n 83) [146], [493];

monopolies over conveyancing work,¹³⁵ and the granting of advocacy rights in higher courts to solicitors (which created competition between solicitors and barristers).¹³⁶ Solicitors were permitted to advertise after 1984. This was a pragmatic response to the fact that licensed conveyancers were able to engage in conveyancing work,¹³⁷ which had been a major proportion of solicitors' work.¹³⁸ The bar followed suit in 1990.

Consistently with the rise of consumerism and competition, in 2000 the Office of Fair Trading turned its attention to arrangements in the legal profession (and other professions) which were said to be anti-competitive. Its 2001 report, *Competition in Professions*, called upon the two branches of the profession either to reform various practices (for example, certain practices relating to advertising), or to explain why they were in the public interest.¹³⁹ The report led to various reforms in both branches of the profession.¹⁴⁰ Here, too, market forces were being introduced directly and purposefully to the legal profession.

Further changes to the legal profession came with the introduction of the Legal Services Act in 2007. This permitted the formation of Alternative Business Structures (firms which can provide both legal and non-legal services, and can be owned and managed by non-lawyers).¹⁴¹ Again, the purposes of the Act included the promotion

ibid 83. Compare Stephen (n 111) 71, who suggests that Thatcher's policies were less about increasing competition than about decreasing the power of all non-governmental institutions.

¹³⁵ Boon (n 61) 83-4.

¹³⁶ ibid 85.

¹³⁷ ibid 66.

¹³⁸ Cyril Glasser, 'The Legal Profession in the 1990s: Images of Change' (1990) 10 *Legal Studies* 1, 4 states that in the mid-1960s, 'Conveyancing provided nearly 60% of the gross income of the profession'.

¹³⁹ Boon (n 61) 88.

¹⁴⁰ ibid 88-9.

¹⁴¹ Legal Services Act 2007 (UK), Part 5. See generally Boon (n 61) 124-31 as to the introduction of the Act, and how it has evolved since its initial introduction.

of competition, and the promotion of interests of consumers.¹⁴² Since 2001, solicitors have been able to incorporate their practices into limited liability partnerships.¹⁴³ Solicitors' firms may thus be largely indistinguishable from any other business.

Since 2013, barristers' standard conditions of contract have enabled barristers to sue for their unpaid fees.¹⁴⁴ Litigants may also now retain barristers directly in certain circumstances (creating further competition between solicitors and barristers).¹⁴⁵ Solicitors are able to pay referral fees in limited circumstances.¹⁴⁶

There has also been external competition. For example, large accountancy firms may provide taxation advice, and advice about business structure and strategy.¹⁴⁷ Large companies have increasingly retained in-house counsel who can perform work previously sent out to law firms, which in effect has created competition between employed lawyers and external firms.

Taking advertising as an example, changes in attitude and changes in regulation have sometimes been mutually reinforcing, creating a 'spiral' of commercialisation. For example, in England the ban on advertising was lifted because the profession feared competition from conveyancers.¹⁴⁸ But, in turn, the introduction of advertising meant that there was now competition *between* lawyers; this focuses attention on the attributes

¹⁴² Legal Services Act 2007 (UK), s 1.

¹⁴³ Solicitors' Recognised Bodies Order 1991/2684; Limited Liability Partnerships Act 2000 (UK); Solicitors' Incorporated Practices (Amendment) Order 2001/645.

¹⁴⁴ The Law Society, 'Instructing a Barrister: New Standard Contractual Terms' (24 January 2013) <<https://www.lawsociety.org.uk/support-services/advice/practice-notes/instructing-a-barrister/>> accessed 20 November 2016, [2.1].

¹⁴⁵ See generally Boon (n 61) 111-12

¹⁴⁶ *ibid* 444-9.

¹⁴⁷ Abel, 'The Politics of Professionalism: The Transformation of English Lawyers at the End of the Twentieth Century' (n 134) 134, 137.

¹⁴⁸ Boon (n 61) 66.

and skills of the individual lawyer, rather than enhancing a sense of collective identity.¹⁴⁹

Removal of civil legal aid

Lawyers' services in the civil jurisdiction are no longer a publicly funded service in England or Australia. The progressive whittling down of civil legal aid in England to its virtual abolition is well-documented.¹⁵⁰ In Australia, civil legal aid was removed in all jurisdictions during the mid-1990s.¹⁵¹

In England, the removal of legal aid was done with the express purpose of opening the legal profession up to market forces.¹⁵² Diminishing availability of legal aid is a clear indication that – for better or worse – legal services for matters in the civil justice system are regarded as something to be privately funded, and subject to market forces.

The commercialisation of the legal profession means that the commodification objection is misplaced

Opposing litigation funding because it adds market values to the legal profession, or to the administration of civil justice, relies on an outdated view of the legal profession. The modern legal profession operates as a market. This is a result of external factors – such as alterations to regulatory provisions – which reflect modern social priorities.

¹⁴⁹ *ibid.*

¹⁵⁰ See, eg, Christopher Hodges, John Peysner and Angus Nurse, *Litigation Funding: Status and Issues (Research Report)* (2012).

¹⁵¹ Law Council of Australia, *Policy Principles: Legal Aid & Access to Justice* (2008), 3.

¹⁵² John Peysner, *Access to Justice: A Critical Analysis of Recoverable Conditional Fees and No Win No Fee Funding* (Palgrave Macmillan 2014), 27-8, 31-3, 37-9.

Even if one were to regard the ‘mercantilisation’ of the legal profession as undesirable, it is now unquestionably entrenched.

Returning to Sandel’s identification of the two vices of commodification, we can say, in the first instance, that litigation funding does not corrupt some value of the civil justice system. There has always been a market for legal services, and it is now the case that access to the legal system is governed by market forces such as competition. Market forces have prevailed. In a similar vein, the removal of civil legal aid has had the clear consequence that access to legal services is more likely to be determined by a party’s means.

It is correct to say that the fact that legal services are commodities creates inequality – the second vice of commodification identified by Sandel. This is because when a service is available for sale in a market, the poor are adversely affected to a greater extent than the rich. However, this has been a problem for as long as legal services have been bought and sold; the ‘anti-market’ era of the legal profession did not restrain this aspect of commodification. It has not been exacerbated by the expansion of market forces; in fact, as explained earlier, some market features – such as the introduction of advertising – may have driven down costs.

Positive consequences of the commodification of legal services?

There are two reasons why one might question whether the commodification of the legal profession is a negative development. First, as was explained earlier in this Chapter, the series of social and regulatory developments which led to the early twentieth century view of legal professional ethics followed a consistent pattern. Over time, the ethical and conduct rules of the legal profession have consistently reflected and reinforced the interests of the upper echelons of the profession. Matters such as the

rejection or denigration of contingency fees, the prohibitions against advertising, and the exhortation to reject ‘money-making trade’ are matters which reinforced the status of the most privileged members of the profession. We can be sceptical about whether these served any broader social purpose, or benefitted clients.

Secondly, the increase in market forces in the legal profession has taken place at the same time as an increased emphasis on, or recognition of, an obligation to engage in pro bono work. It is possible that market forces have, in fact, facilitated the increased emphasis on pro bono work.

In the United States, Pearce has suggested that the increased focus on pro bono work has been both a product and cause of the diminution of the traditional view of legal professional ethics. He notes that the idea that there was a distinct pro bono duty emerged only in the 1970s,¹⁵³ and the fact that this was treated as a discrete obligation meant that lawyers could effectively reconcile a commitment to public interest with the pursuit of the interests of themselves and their clients.¹⁵⁴ In other words, the emergence of a discrete pro bono duty served, in effect, to discharge the general obligation to pursue the public interest.

In England and Australia too, there is a perception within the legal profession that pro bono work for the benefit of the disadvantaged is part of the professional obligation of a lawyer. Indeed, both the Law Society of England and Wales and the Law Council of Australia have adopted public statements to the effect that whilst pro bono services are no substitute for government-funded legal aid, pro bono work is nevertheless a valuable and desirable aspect of legal practice, which is to be

¹⁵³ The 1970 ABA Code of Professional Responsibility encouraged lawyers to ‘find time to participate in serving the disadvantaged’.

¹⁵⁴ Pearce (n 64) 419-20.

encouraged.¹⁵⁵ The obligation to assist in providing access to justice seems to be accepted, at least by some sectors of the legal profession, as part of the professional self-identity of lawyers. This may be contrasted with the position described by Gurney-Champion in 1926, when lawyers did not regard pro bono work as ‘a desirable thing or an honourable thing’.¹⁵⁶

Firms also engage in pro bono work as an aspect of corporate social responsibility (in which they take pride).¹⁵⁷ Outside the traditional pro bono sphere of legal assistance to the impecunious, large firms of solicitors may also provide low-cost services to community organisations which are sponsored by their corporate clients, thus reinforcing their client relationships.¹⁵⁸ Pragmatically, pro bono work may also serve as an employee-retention tool; it can enable more junior solicitors to gain

¹⁵⁵ See Law Society, ‘Pro Bono Policy’ <<https://www.lawsociety.org.uk/topics/pro-bono/pro-bono-policy>> accessed 31 July 2020; Law Council of Australia, *Submission to the Productivity Commission* (2013), [506]-[509]. See also Australian Government Productivity Commission, *Access to Justice Arrangements (Productivity Commission Inquiry Report No 72)* (2014), Chapter 23.4, ‘What impacts on lawyers’ willingness and capacity to provide services?’ The Productivity Commission introduces that section of the report by noting that ‘Pro bono service provision has been, and to a large extent still is, motivated by a lawyer’s sense of professional responsibility.’

¹⁵⁶ Gurney-Champion (n 90) 8; see also 17; the full quote is set out at the text accompanying footnote 125 above.

¹⁵⁷ Law firms often advertise their pro bono work on their websites: the websites of the five ‘Magic Circle’ solicitors’ firms in London provide excellent examples of this: see Allen & Overy, ‘Pro Bono and Community Investment’ <https://www.allenoverly.com/en-gb/global/about_us/corporate_responsibility/pro_bono_and_community> accessed 31 July 2020; Clifford Chance, ‘Community & Pro Bono - Access to Justice’ <https://www.cliffordchance.com/about_us/responsible-business/community-and-pro-bono/access-to-justice.html> accessed 31 July 2020; Linklaters, ‘Social Impact - Acting for Asylum Seekers in London, Hong Kong and New York’ <<https://www.linklaters.com/en/about-us/responsibility/social-impact/acting-for-asylum-seekers-in-london-hong-kong-and-new-york>> accessed 31 July 2020; Freshfields Bruckhaus Deringer, ‘Pro Bono’ <<https://www.freshfields.com/en-gb/about-us/responsible-business/pro-bono/>> accessed 31 July 2020; Slaughter and May, ‘Pro Bono’ <<https://www.slaughterandmay.com/our-firm/responsible-business/pro-bono/>> accessed 31 July 2020.

¹⁵⁸ Australian Government Productivity Commission (n 155) 810.

exposure to a more diverse range of work, or to take a leading role on a file where they might usually only work as a junior member of a team.¹⁵⁹

In some Australian jurisdictions, governments have sought encourage this more formally. For example, firms which wish to tender to provide legal services to either the Federal government or the Victorian government are required to commit to a ‘pro bono aspirational target’.¹⁶⁰ Accordingly, in considering Australia’s access to justice arrangements, the Productivity Commission – in a chapter devoted to the role of pro bono services – recommended that the larger Australian jurisdictions should consider adopting similar requirements.¹⁶¹

Thus, market forces might have created a new reason for lawyers to engage in pro bono work. Simply put, it might be good for business – for example, by enabling firms to support the charitable work of their corporate clients, and providing desirable experience to junior solicitors. Whilst this evidence is not conclusive, it gives pause for thought in thinking about whether there might be an access to justice benefit in market forces. One might say that the profession’s commitment to the public interest has evolved from high-minded statements of principle (which had questionable benefit to the public interest) to more limited, but more practical and tangible contributions (such as through pro bono work).

¹⁵⁹ *ibid* 817.

¹⁶⁰ *ibid* 833, 837 explains the nature of the different systems which are implemented by the Federal government and the Victorian government.

¹⁶¹ *ibid* 836-7. See generally Chapter 23 concerning pro bono services. The Law Council of Australia was more reticent about the utility of such schemes: see Law Council of Australia, *Submission to the Productivity Commission* (2013), [508].

Conclusion

There are two aspects to the commodification objection. First, there is concern about the creation of markets in causes of action. Secondly, there is the concern about the introduction of market forces to the legal profession, or to the civil justice system.

Each concern is misplaced. The two vices of commodification are that it can serve to corrupt some value, and that it can serve to create or reinforce inequality between rich and poor. Litigation funding does not suffer from either of these problems.

In relation to the market for causes of action, the question whether some value or good is corrupted depends critically on what one considers to be the primary value of the civil justice system. As I explained in Chapter 3, the pre-eminent value of the civil justice system is to enforce the rule of law; for the reasons there explained, litigation funding advances this value. In fact, a market for causes of action might serve to reduce (not to increase) inequality, because it means that a cause of action is an asset which an impecunious claimant can exploit to their advantage.

In relation to the market for legal professional services, we can see that commercial values and market forces now dominate the legal profession, as a result of externally-imposed regulatory changes. This means that there is little risk that litigation funding will corrupt the status quo.

Having discussed the principled objections to litigation funding, we may now turn to developing a positive concept of the role that litigation funding plays in the civil justice system, and the practical matters of the potential risks (and how those ought to be regulated). To set the groundwork for this, the following chapter will explain the present state of the litigation funding market.

CHAPTER 6: THE EMERGING MARKET FOR LITIGATION FUNDING

Introduction

This chapter provides an overview of the commercial litigation funding market. First, I address the typical features of litigation funding agreements. Secondly, I identify the criteria which funders use to select cases. Finally, I describe the forms of funding which exist in the market.

Usual terms of litigation funding

At its most simple, commercial litigation funding entails a funder paying for a claimant's legal costs in exchange for a share in the proceeds of any judgment or settlement. Although litigation funding agreements are usually confidential, information about typical terms is freely available from funders.¹ Because the industry is in a nascent stage, and has been historically controversial, it has been in funders' interests to share this information – to educate potential clients, and to demonstrate the legitimacy of the industry through transparency.²

Standard matters dealt with in the litigation funding contract are:³

¹ In addition to publications by funders, this chapter refers to practitioner texts, academic works and law reform commission reports. However, the information in these sources is ultimately derived from funders. In reporting on the market practices of funders, I frequently refer to articles written by Burford, which is the world's largest provider of litigation funding; however, a review of other funders' materials indicates that their approach is broadly representative (and I have sought to identify divergences in market practice where they arise).

² See, eg, Burford, 'Yes, Legal Finance is at an Inflection Point—But not the One you Think' (4 December 2018) <<http://www.burfordcapital.com/blog/yes-legal-finance-is-at-an-inflection-point-but-not-the-one-you-think/>> accessed 5 May 2019.

³ Nick Rowles-Davies, *Third Party Litigation Funding* (Jeremy Cousins QC ed, Oxford University Press 2014), [1.29]; see also Leslie Perrin, 'England and Wales' in Leslie Perrin (ed), *The Third Party Litigation Funding Law Review* (Law Business Research Ltd 2018), 52-3.

- identifying the solicitors and barristers who will work on the claim (who may even be parties to the agreement);
- the budget for the claim;
- the return to the funder in the event of success;
- the circumstances which will be treated as ‘success’; and
- the circumstances in which the funding agreement may be terminated.

Funding is usually provided on a non-recourse basis.⁴ This means that if litigation is unsuccessful, the claimant will not be required to reimburse the funder for its investment in the litigation – or, in other words, that the funder has no recourse to the claimant for its investment in the litigation.

Funder’s return

In the event of success in the litigation (either by judgment or settlement), it is usual that the funder has its investment returned to it (i.e. its expenditure on unrecoverable legal costs and disbursements),⁵ and that this comes out of the proceeds first.⁶ The funder will also receive an element of profit. The profit may be calculated as a percentage of the investment (say, three times the expenditure on legal costs), or as a percentage of the proceeds (say, 30% of any net proceeds of the settlement or

⁴ Rowles-Davies (n 3) [1.21]; Burford, ‘Q&A with Craig Arnott: The Rise of Legal Finance in Asia-Pacific’ (9 April 2019) <<http://www.burfordcapital.com/blog/interview-legal-finance-growth-asia-australia/>> accessed 5 May 2019.

⁵ By ‘unrecoverable’ costs, I refer to the gap between the actual expenditure on legal costs, and the likely recovery of party-party costs in the event of success.

⁶ Burford, ‘A Legal Finance Primer for Legal Operations and Law Firm Pricing Professionals’ (30 April 2019) <<http://www.burfordcapital.com/blog/legal-finance-primer-operations-pricing/>> accessed 5 May 2019; Burford, ‘Pricing Risk, Structuring Agreements and the Cost of Legal Finance Capital’ (14 November 2018) <<http://www.burfordcapital.com/blog/pricing-risk-structuring-agreements-cost-legal-finance-capital/>> accessed 5 May 2019.

judgment).⁷ In England and Australia, it is more common to have a percentage; the use of a multiple of the investment is more common in the US.⁸

There are many variations.⁹ For example, the return might be a percentage of the investment *plus* a percentage of the proceeds (say, twice the expenditure plus 10% of net proceeds).¹⁰ Or, the funder's profit might be expressed as an alternative, with one calculation acting as a 'floor' – such as X times the investment, or Y percentage of the proceeds, whichever is greater.¹¹

Where the profit is calculated as a percentage, it might increase or decrease incrementally – say X% for the first £5 million of any net proceeds, and Y% of any proceeds thereafter. The percentage might increase as time wears on, so that, for example, the funder receives X% if the matter is finalised within a year, and Y% if it is finalised after that date – reflecting the fact that the funder has been out of pocket for a longer period. These percentages may be used to incentivise the claimant, so that their interests are aligned with the funder – for example, by structuring the returns so that the claimant receives a higher percentage if the matter settles early, if that is in the funder's interests.¹² Finally, in class actions, it is possible for different groups of claimants within a single action to be charged different percentages. So, for example, in a

⁷ Ibid.

⁸ Andrew Saker and Diane Jones, 'Litigation Funding Masterclass' (*IMF Bentham*, October 2015) <<https://www.imf.com.au/docs/default-source/site-documents/investor-presentation---litigation-funding-masterclass360804010281659d9b61ff00006a85af>> accessed 16 July 2019, 3.

⁹ See generally Rowles-Davies (n 3) [1.20], [5.74]-[5.86].

¹⁰ Burford, 'A Legal Finance Primer for Legal Operations and Law Firm Pricing Professionals' (n 6); Burford, 'Pricing Risk, Structuring Agreements and the Cost of Legal Finance Capital' (n 6).

¹¹ See, eg, David Marin-Guzman, 'A Real Worry: Judge Slams Litigation Funding Fees' *Australian Financial Review* (30 May 2019) <<https://www.afr.com/leadership/workplace/a-real-worry-judge-slams-litigation-funding-fees-20190529-p51sao>> .

¹² Rowles-Davies (n 3) [5.85]-[5.86].

shareholder class action, the percentage might be higher for claimants with a smaller number of shares, and lower for large shareholders.¹³

The terms offered by a funder depend on the level of risk assumed.¹⁴ According to Burford, the assessment of risk takes into account the merits of the litigation, the stage it has reached (with unfiled or just-filed claims the highest risk), the anticipated recovery, and the diversification of risk (with single-case funding being higher risk than a portfolio; portfolio funding is explained below).¹⁵ The price of funding also takes into account the ‘time element’ – that is, the fact that there might be several years between the funder’s investment and any return.¹⁶ The cost of funding also takes into account matters internal to the funder, such as its own cost of money and overheads.¹⁷

Liability for adverse costs

In practice, it appears that English funders do not necessarily assume liability for adverse costs as a matter of course,¹⁸ but may do so.¹⁹ However, the funder might be liable as a third party in any event.²⁰

¹³ See, eg, *Earglow Pty Ltd v Newcrest Mining Limited* [2016] FCA 1433 [160].

¹⁴ Burford, ‘A Legal Finance Primer for Legal Operations and Law Firm Pricing Professionals’ (n 6).

¹⁵ *ibid*; Burford, ‘Pricing Risk, Structuring Agreements and the Cost of Legal Finance Capital’ (n 6).

¹⁶ Burford, ‘Five minutes with... Elizabeth O’Connell’ (9 November 2018) <<http://www.burfordcapital.com/blog/five-minutes-with-elizabeth-oconnell/>> accessed 5 May 2019; Rowles-Davies (n 3) [5.82]-[5.83].

¹⁷ Rowles-Davies (n 3) [5.78].

¹⁸ Although cf Therium, ‘Frequently Asked Questions’ <<https://www.therium.com/frequently-asked-questions/>> accessed 10 May 2019.

¹⁹ Perrin (n 3) 52.

²⁰ *ibid*.

In *Arkin*, the Court of Appeal limited a commercial funder's exposure to adverse costs to the quantum of funding they have provided to the claimant.²¹ The Arkin cap was applied virtually as a matter of course for many years. However, in *Chapelgate v Money*,²² it was confirmed that the Arkin cap ought not to be applied mechanically, so that the extent of the funder's liability is still a matter for the discretion of the court. The principles upon which the court will order costs against the funder are discussed in detail in Chapter 7.

If the funder does not assume liability, the claimant's exposure to adverse costs may be covered by after-the-event insurance ('ATE') if desired, and the funder's own liability as a third party will need to be covered, either by insurance, or a higher percentage of the proceeds.²³

In Australia, funders agree to pay for adverse costs as a matter of course. The court has power to order costs against the funder (in the exercise of its power to order costs against a third party), but there is no equivalent of the *Arkin* cap. One would expect that Australian funders would take the adverse costs exposure (or the cost of their own insurance to cover such costs exposure) into account in pricing funding.

Budget

In making a decision whether to fund, funders will require a costs budget, both for the claimant's costs and for the opponent's anticipated costs.²⁴ In the event that the claim

²¹ *Arkin v Borchard Lines (Nos 2 and 3)* [2005] EWCA Civ 655; [2005] 1 WLR 3055, [41].

²² *Chapelgate Credit Opportunity Master Fund Ltd v Money* [2020] EWCA Civ 246.

²³ Burford, 'Adverse costs and insurance' (31 May 2017) <<http://www.burfordcapital.com/blog/adverse-costs-insurance/>> accessed 6 May 2019.

²⁴ Rowles-Davies (n 3) [1.39], [5.36]-[5.41]; Lisa Bench Nieuwveld and Victoria Shannon Sahani, *Third-Party Funding in International Arbitration* (2nd edn, Kluwer Law International 2017), 31.

fails, the funder – having already paid for the claimant’s costs – will lose this investment, because funding is provided on a non-recourse basis. The funder will almost certainly be required to pay adverse costs – either because of a term in the funding contract, or by operation of the court’s power to order that costs be paid by a third party. The costs budget therefore represents the extent of the funder’s exposure to risk.²⁵

The commerciality of a litigation funding business therefore depends on ensuring, for each funded claim, that costs are proportionate to the likely return, and, across the business, that the funder’s return on winning claims is sufficient to cover its losses on losing claims. The use of a budget for costs, and the calculation of the return in the event of success, are therefore critical.

In England, it is usual for costs to be capped, or for the lawyer to act on a conditional fee agreement (CFA).²⁶ If there is a cap, then there might be some provision for the lawyers to benefit in the event of success, in exchange for taking the risk that their costs may exceed the cap.²⁷ For example, it may be the case that the funder will pay costs up to the cap, with the solicitors to work on a conditional fee basis thereafter.²⁸

The sample Therium agreement in Rowles-Davies’ book is instructive as to how funds are deployed, and the operation of the cap. The funder has assumed the obligation to pay reasonable costs in respect only of the first tranche of the litigation, and has the option to fund subsequent tranches.²⁹ A cap is provided in respect of each tranche.

²⁵ Bench Nieuwveld (n 24) 32.

²⁶ Rowles-Davies (n 3) [5.87].

²⁷ Bench Nieuwveld (n 24) 32.

²⁸ *Earglow* (n 13) [179(c)] (dealing with Australian class actions).

²⁹ Rowles-Davies (n 3) Appendix 1, [2.1].

There is also provision for variations to the contract to be agreed.³⁰ Funders are ‘uniformly resistant to overspend on foreseeable items’, but it is common for there to be some variation in the budget as time progresses, both to accommodate contingencies, and to ensure that the expenditure reflects the merits of the claim as they emerge.³¹ In the Australian class action context, examples of cases can be found in which funders have continued to fund, despite the cap having been reached.³²

How cases are selected

Due diligence

Due diligence enables the funder to determine whether to fund, and the terms on which funding will be offered.³³ The criteria which are relevant to the question whether to fund are also relevant to the price of funding if it is offered.³⁴ The precise process varies between funders.³⁵ In order to conduct due diligence, claimants must share key documents from the litigation, as well as a budget to enable an assessment of the economics of the proposed investment.³⁶ This requirement to provide documents can be onerous for claimants and their lawyers.³⁷ Burford advises that due diligence usually

³⁰ *ibid* [19].

³¹ Bench Nieuwveld (n 24) 32.

³² *Earglow* (n 13) [180].

³³ Bench Nieuwveld (n 24) 38-9.

³⁴ See *ibid* 34 for a list of matters relevant to the value of an arbitration claim, many of which are equally applicable to a litigation claim.

³⁵ See Rowles-Davies (n 3) Chapter 5 for the general process.

³⁶ Burford, ‘Demystifying the Litigation Finance Diligence Process’ (18 September 2017) <<http://www.burfordcapital.com/blog/demystifying-litigation-finance-diligence/>> accessed 6 May 2019; Rowles-Davies (n 3) [5.28]-[5.30].

³⁷ Bench Nieuwveld (n 24) 23, 39.

takes about four to six weeks, although for late-stage matters (such as appeal funding) it may be as little as 7 to 10 days.³⁸

The claimant and funder will execute a non-disclosure agreement in order to protect the confidentiality of documents provided to the funder. The mere existence of the funding agreement and the funder's identity will not be privileged. Beyond that, in England it is accepted that common interest privilege will apply to documents supplied to the funder.³⁹

Funders will typically assess the merits of a case using their own staff,⁴⁰ although the opinions of counsel may be relevant in this process. These staff will also determine the price of funding. At most funders, cases which are sufficiently meritorious will be put to an investment committee, which makes the final approval decision.⁴¹

Funders will often insist on exclusivity,⁴² although this is not universal.⁴³ Funders may be more likely to seek exclusivity if they will incur the cost of external counsel during due diligence.⁴⁴

³⁸ Burford, 'Demystifying the Litigation Finance Diligence Process' (n 36).

³⁹ Perrin (n 3) 53

⁴⁰ Rowles-Davies (n 3) [4.68]-[4.69] (Burford), [4.79] (Therium), [4.86]-[4.87] (Vannin).

⁴¹ Rowles-Davies (n 3) [4.71] (Burford), [4.79] (Therium), but cf Vannin [4.86]-[4.87], where the investment committee itself performs the review.

⁴² Rowles-Davies (n 3) [5.60]-[5.64]; Bench Nieuwveld (n 24) 22.

⁴³ Eg, Burford does not seek exclusivity— see Burford, 'A Legal Finance Primer for Legal Operations and Law Firm Pricing Professionals' (n 6).

⁴⁴ Rowles-Davies (n 3) [5.05], [5.61].

Criteria for selecting cases

The overarching consideration for commercial litigation funders, in selecting which cases to fund, is to maximise their return and minimise their risk. This overarching consideration translates into a series of specific criteria.

Is the claimed sum recoverable?

First, the capacity of the defendant to pay is critical.⁴⁵ For example, professional negligence claims are attractive to funders, because the defendants are likely to be insured.⁴⁶ Funders are also concerned to ensure that any judgment will be recoverable. This entails a consideration of the location of the defendant's funds (eg, onshore or offshore, or in a trust structure), and the ease of enforcement procedures.⁴⁷

Is there a good claim?

The merits of the claim are obviously critical.⁴⁸ One aspect is whether the claim rests on well-established legal principles.⁴⁹ The claim must usually be one which will, if successful, require the defendant to pay money to the claimant, rather than some other form of relief.⁵⁰

Most funders will invest in litigation across a wide range of commercial claims.⁵¹ However, it is common for funders to refuse to consider funding applications

⁴⁵ Rowles-Davies (n 3) [1.51].

⁴⁶ *ibid* [1.52], [3.52], [5.34].

⁴⁷ *ibid* [5.35].

⁴⁸ Burford, 'Q&A with Craig Arnott: The Rise of Legal Finance in Asia-Pacific' (n 4); Burford, 'Demystifying the Litigation Finance Diligence Process' (n 36); Rowles-Davies (n 3) [3.40].

⁴⁹ Rowles-Davies (n 3) [1.54].

⁵⁰ *ibid* [1.49]-[1.50].

⁵¹ *ibid* [3.33]-[3.34].

in personal injury or matrimonial matters.⁵² Funders are less interested in claims which rely heavily on witness testimony, owing to the unpredictability of witness performance in court.⁵³

In assessing the risks of a case, a funder will consider matters including:⁵⁴

- whether the case turns on the credibility of competing witnesses;
- whether there is more than one ‘case theory’ that supports the claimant’s case;
- the strength of the legal basis for the claim; and
- whether the ‘case theory’, and the extent of the damages, is plausible in the commercial context,

Is the claimed sum sufficiently large to ensure that the funding agreement is commercial?

Thirdly, the funding agreement has to make commercial sense for both parties. There must be proportionality between anticipated expenditure and anticipated recovery, and the recovery has to be large enough to accommodate a commercial return to both the funder and the claimant. There are two reasons for this.

First, in the event of success, the funder will usually be reimbursed for its expenditure (i.e. the amount paid in unrecoverable legal costs),⁵⁵ and also receive a percentage of the remaining proceeds. The percentage represents the element of profit.

⁵² Bench Nieuwveld (n 24) 76. See, eg, Therium, ‘Frequently Asked Questions’ (n 18); Rowles-Davies (n 3) [4.77].

⁵³ Rowles-Davies (n 3) [3.41].

⁵⁴ Burford, ‘Demystifying the Litigation Finance Diligence Process’ (n 36).

⁵⁵ As to the meaning of ‘unrecoverable costs’, see footnote 5 above.

The funder's profit therefore depends on the value of the claim. If a funder spends, say, £400,000 in unrecoverable legal costs, to recover a judgment of £1 million, and is entitled to a 30% success fee, then its profit will be £180,000 (i.e. 30% of the £600,000 net proceeds). The funder will have made a 45% return on its investment. The commerciality of this return will depend on the funder's own cost of capital, the time that the funder must wait for its return – and, of course, how frequently the funder is successful across its entire portfolio of cases, bearing in mind that if the funded claim is unsuccessful, it may well have to pay adverse costs, too.

Secondly, there is a need to ensure that the claimant remains motivated.⁵⁶ If the claimant's recovery is likely to be swallowed up by unrecoverable legal costs, and the funder's profit, the claimant may be insufficiently motivated to pursue its own claim with sufficient vigour. It is therefore commercially rational for the funder to ensure that a funding agreement makes commercial sense for the claimant, too. In the scenario set out above, for example, the claimant would receive only £420,000 of a £1 million claim.

Clearly, the commerciality will be affected if the costs budget is exceeded, and/or if the recovery (by settlement or judgment) is less than anticipated, and/or if the amount received in costs in the event of success is less than anticipated. The effect of any variance in these factors will be more acute for smaller claims.

Therefore, funders will ensure that there is some proportionality between the likely costs, and their return – which, in turn, is linked to the value of the claim.⁵⁷ The mainstream of the funding industry is focused on large-value claims for this reason. In

⁵⁶ This consideration may be less weighty in class actions. For this reason, there may be a greater risk in class actions that funders will seek a percentage return which leaves the claimant with a relatively small share in any success.

⁵⁷ Rowles-Davies (n 3) [3.43]-[3.45].

2014, Rowles-Davies reported that at a minimum, funders would seek claims in the range of £3 million - £5 million,⁵⁸ and would want the budgeted expenditure to likely damages to have a minimum ratio of 1:4, but more commonly 1:10.⁵⁹ Whilst some funders eschew any suggestion that there is a particular ratio of funding to claim value, Harbour has indicated that where a claim has a value less than £20 million, it would be usual to require that the value of the claim is at least 10 times the amount required in funding.⁶⁰ Burford has said that economics of funding work best when funding is provided in an amount of \$2 million or more, and that most of its cases are funded to an amount between \$4 million and \$10 million. It, too, provides an indicative ratio of 10 times investment to damages.⁶¹ Therium has indicated that it seeks cases in which the damages will be 6 to 10 times its investment.⁶² Vannin seeks claims over £5 million, with a 10:1 ratio of claim to budgeted costs.⁶³ Most mainstream funders are thought to seek a profit return of at least three times their expenditure.⁶⁴

Choice of lawyers

Confidence in the solicitors and barristers who have been engaged by the litigant is also a criterion.⁶⁵ In class actions, though, it may be that the solicitor and/or funder

⁵⁸ *ibid* [3.44].

⁵⁹ *ibid* [1.48], [3.44].

⁶⁰ Harbour Litigation Funding, 'Our Criteria' <<https://www.harbourlitigationfunding.com/how-we-work/our-criteria/>> accessed 9 May 2019.

⁶¹ Burford, 'Demystifying the Litigation Finance Diligence Process' (n 36).

⁶² Therium, 'Frequently Asked Questions' (n 18).

⁶³ Rowles-Davies (n 3) [4.85].

⁶⁴ *ibid* [2.21].

⁶⁵ Burford, 'Q&A with Craig Arnott: The Rise of Legal Finance in Asia-Pacific' (n 4); Burford, 'Demystifying the Litigation Finance Diligence Process' (n 36); Therium, 'Frequently Asked Questions' (n 18); *ibid* [3.39], [5.42]-[5.43].

investigate a potential claim and recruit claimants. The significance of this aspect of practice is discussed in Chapter 11.

How far has the litigation progressed?

Funding may be provided at any stage of a claim. Funders may even provide funding *after* a judgment or settlement, to enable a claimant to benefit from their winning without waiting for court approval or enforcement.⁶⁶ In the case of a claimant who has won a judgment in their favour, post-judgment finance will enable them to transfer to the funder the risk of losing, or having their judgment reduced, on appeal.⁶⁷ Such funding may be in addition to providing funding for the costs of appeal.⁶⁸

The likely time to resolution of the claim – by settlement or judgment – is also relevant. Even if the claim is successful, the funder will have paid costs for the duration of the proceedings, which may be many years. It will only obtain a return if and when the claim is successful, and there is some recovery by the claimant. For the duration of the proceedings, therefore, there is an opportunity cost to the funder in making an investment – i.e. paying lawyers' fees – with no return. Funders will therefore prefer a case which is likely to resolve quickly,⁶⁹ and the anticipated duration will be taken into account in the cost of funding.⁷⁰

⁶⁶ Burford, 'Monetizing Judgments to Optimize Cash Flow' (18 September 2018) <<http://www.burfordcapital.com/blog/monetizing-judgments-optimize-cash-flow/>> accessed 6 May 2019.

⁶⁷ Burford, 'Financing Judgments and Settlements: Advantages & Considerations' (31 May 2018) <<http://www.burfordcapital.com/blog/financing-judgments-settlements-advantages-considerations/>> accessed 6 May 2019.

⁶⁸ *ibid.*

⁶⁹ Rowles-Davies (n 3) [1.53].

⁷⁰ *ibid* [3.48].

What is the claimant's motivation?

Another matter which is important to funders is the general motivation and risk profile of the claimant.⁷¹ Because the funder is making an investment that they cannot control (in England, at least), then the funder will want to be satisfied that the claimant will make rational and commercial decisions as the case progresses.⁷² It is for this reason that insolvency practitioners are desirable customers for funders.⁷³ This is likely to be less of an issue in Australian class actions (for example), where the funder exerts more control over the litigation.

Funders may affect the motivation of claimants by careful structuring of the funding agreement. So, for example, if the matter is one where an early settlement is particularly desirable, then the funder could structure the terms so that the return to the claimant is greater on an early settlement than if the matter proceeds to trial.

Thus, whilst much is sometimes made of the differences between Australian and English law in terms of the control exerted by the funder, the differences may be more apparent than real. English funders are able to ensure that claimants have interests which are aligned with theirs, through consideration of the claimant's motivations, and structuring the funding agreement – even if overt control, in the Australian mould, is impermissible.

⁷¹ Bench Nieuwveld (n 24) 41.

⁷² Rowles-Davies (n 3) [1.38], [3.37]-[3.38].

⁷³ See the text accompanying footnotes 79 and 80.

Claims by insolvency practitioners – what is the size of the creditor pool?

One funder has suggested that there is an additional consideration in insolvency matters: namely, the size of the creditor pool relative to the size of the claim. As the funder explained it:⁷⁴

... you could have a claim for \$200 million, but if the amount that is owed to creditors is, let's say, \$50 million, then that is likely to be the driver for any settlement amount. Because any sensible defendant will look at the amount of creditors and say, 'well, if they can come out whole, they should be happy, so I could settle this claim at a lower amount than the headline value'.

Forms of funding

The litigation funding market has expanded rapidly in recent years. In this section, I set out forms of funding which are available and emerging in England and Australia.

Single case funding

Companies in insolvent administration

A company in insolvent administration may have valuable causes of action. But it is in a weak position in seeking to enforce its rights. It cannot exert market pressure upon those owing obligations to it. Secondly, it may have limited funds – if any – available for litigation. Thirdly, the company's funds are ultimately to be distributed to creditors. The cost of litigation – and its risk – will thus be borne, in effect, by the creditors.

It is therefore unsurprising that legislation in England and Australia, (as well as other jurisdictions, including Hong Kong) permitted an administrator of an insolvent company to sell its causes of action as an asset. The insolvency context is a long-

⁷⁴ Susan Dunn, 'Third Party Funding for Insolvency Claims – Part 2 – Liquidators, Insolvency Claimants & Funders' Criteria' (*Conventus Law*, 19 April 2018) <<https://www.youtube.com/watch?v=g2GXxVTsOtw>> accessed 10 May 2019.

standing exception to the prohibition against maintenance and champerty.⁷⁵ Thus, litigation funding in the insolvency context was clearly lawful even at a time when its legitimacy in other contexts was doubtful.

Insolvency litigation provided the genesis of the modern litigation funding industry in Australia.⁷⁶ Much Australian judicial discussion of the merits and demerits of litigation funding has taken place in the context of insolvency. This is because a liquidator must seek the court's approval before entering into a funding agreement.⁷⁷

Litigation by companies in insolvent administration serves a valuable role in private law enforcement. It is not uncommon for liquidators to cause insolvent companies to bring proceedings of the sort that a corporate regulator might have brought. Where the wrongdoing of a former officer, or the unconscionable receipt of the company's assets by a third party, has led to the very insolvency which necessitates the use of funding, there is clearly a strong interest in proceedings being brought, so that the law is enforced.⁷⁸

Insolvency practitioners are extremely attractive clients for litigation funders. In part, this is because they are experienced in conducting litigation, and are commercially minded in their approach.⁷⁹ Further, they are driven by securing the best

⁷⁵ See Chapter 2 as to the history of the insolvency exception.

⁷⁶ Bench Nieuwveld (n 24) 77.

⁷⁷ The criteria for approval are discussed in Chapter 9.

⁷⁸ *Re Pantmaenog Timber* [2004] 1 AC 158 (HL).

⁷⁹ Susan Dunn, 'Third Party Funding for Insolvency Claims – Part 1 – About Funders and Insolvency Claims' (*Conventus Law*, 19 April 2018) <<https://www.youtube.com/watch?v=81m80SeEMWU>> accessed 10 May 2019.

outcome for creditors – that is, to maximise the value of the claim, rather than to vindicate their position – and so their interests are aligned with that of the funder.⁸⁰

Impecunious claimants

The position of the impecunious claimant receiving funding for a single case is well-represented in the literature on litigation funding. Again, the provision of funds to people of limited means was always an exception to the prohibition on maintenance and champerty. However, it is critical to observe that this market is *not* pre-eminent in England or Australia. As explained earlier, the dominant model of litigation funding in England and Australia entails that funders take on a small number of large-value cases, and perform extensive due diligence to ensure that these cases are worthy of investment.

Nevertheless, there are a small number of funders, even in England and Australia, who focus on smaller-value claims. It might be expected that this market will grow, as the litigation funding market expands, and funders are driven to expand beyond high value claims in order to expand their businesses. Of course, outside the commercial context, the case law on litigation funding provides numerous examples of litigation in which a third party has funded a small claim on an ad hoc basis – for example, for charitable purposes, or for the benefit of a family member. One question that must be addressed in the context of regulation is whether, and to what extent, this sort of arrangement ought to be captured in regulation.

Obvious risks that exist in this context arise from the fact that an impecunious claimant has limited bargaining power. This may arise because of their need for funding, and the absence of alternative sources. It may also arise because of their

⁸⁰ Dunn 'Third Party Funding for Insolvency Claims - Part 2 – Liquidators, Insolvency Claimants & Funders' Criteria' (n 74).

inexperience in litigation. Accordingly, they might be vulnerable to a funder imposing uncommercial terms.⁸¹ Further, impecunious claimants are particularly susceptible to the funder's continued ability and willingness to fund the litigation as it proceeds. If the funder runs out of funds, or terminates the funding agreement, then an impecunious claimant will, *ex hypothesi*, be unable to continue, and will be unable to bear the burden of their opponent's costs.

Well-resourced but risk-averse claimants

Even a well-resourced claimant may not wish to fund its own litigation. Civil litigation is notoriously expensive and unpredictable. Cost-shifting rules introduce further expense and unpredictability.

Civil litigation can also be time-consuming, and can divert the officers of corporate claimants from more economically rewarding activities. Even sophisticated and well-resourced claimants may not be experienced in the conduct of litigation. If a funder will provide some guidance, or perhaps even exert a degree of control over the day-to-day conduct of the litigation, that may be a further benefit to such a claimant.

For such claimants, litigation funding presents an opportunity to have a chance of recovery without any need to incur legal fees (albeit at the cost of sharing any recovery). Litigation funding is, therefore, a valuable tool for avoiding the risks of litigation, even for those who can afford litigation.⁸²

⁸¹ Poonam Puri, 'Profitable Justice: Aligning Third-Party Financing of Litigation with the Normative Functions of the Canadian Judicial System' (2014) 55 *Canadian Business Law Journal* 34, 36.

⁸² Rowles-Davies (n 3) [1.56]-[1.58]; see generally Lee Drucker, 'A Financial Perspective on Commercial Litigation Finance' (2015) 12 *New York University Journal of Law and Business* 665; Joanna M Shepard and Judd E Stone, 'Economic Conundrums in Search of a Solution: The Functions of Third-Party Litigation Finance' (2015) 47 *Arizona State Law Journal* 919, 923-9.

It is clear that there can be significant benefits to the use of funding even to well-resourced claimants, and also clear that funders are marketing to this group. The benefits that funders point to are two-fold.

First, even in large commercial enterprises, the budget for legal expenses is limited, and the cost and unpredictability of litigation are a deterrent to litigation, even for these well-resourced claimants.⁸³

Secondly, the use of litigation funding by large corporates has the effect of removing an expense – i.e. legal expenses – from the company’s profit and loss statement. The decrease in operating expenses, and the corresponding increase in reported profits, can improve the market value of the company.⁸⁴

The accounting treatment is as follows. In the absence of litigation funding, legal expenses are treated as expenses of the company, which reduce earnings (and therefore EBITDA, a common measure of a company’s profitability). However, any proceeds of litigation are treated as a non-recurring or extraordinary item, and therefore do not improve EBITDA.⁸⁵ Legal expenses therefore decrease profitability, even if the litigation is ultimately successful.

Litigation funding improves the balance sheet. As an example, Burford reports that it provided a FTSE 20 company – widely reported to be BT⁸⁶ – with £40 million

⁸³ Burford, ‘2018 Litigation Finance Survey’ (2018) <<http://www.burfordcapital.com/wp-content/uploads/2018/10/Burford-Capital-2018-Litigation-Finance-Survey.pdf>> , esp 11-12, 32, 45.

⁸⁴ Burford, ‘Five minutes with... Elizabeth O’Connell’ (n 16).

⁸⁵ Burford, ‘Portfolio Financing for In-House Legal Departments’ (2 October 2018) <<http://www.burfordcapital.com/blog/portfolio-financing-in-house-legal-departments/>> accessed 6 May 2019.

⁸⁶ See, eg, Tabby Kinder, ‘BT Signs \$45m Litigation Funding Deal with Burford Capital’ (*The Lawyer*, 26 January 2016) <<http://www.thelawyer.com/bt-signs-45m-litigation-funding-deal-with-burford-capital/>> accessed 17 February 2016.

in non-recourse finance, linked to a portfolio of claims. The company was able to use the funds for legal expenses or other activities, as it chose. The funds advanced were treated as income, therefore improving its EBITDA.⁸⁷

The use of funding to improve a company's balance sheet is a nascent area in Australia, which is anticipated to grow in coming years.⁸⁸

Conventional arguments for and against litigation funding are of little application here. First, concerns about the exploitation of funded claimants are likely to be of less relevance where the claimant is a sophisticated corporate entity. On the other hand, the conventional argument that litigation funding has value insofar as it promotes access to justice for the impecunious is also largely inapplicable here – commercial claimants may well have sufficient funds to engage in litigation, and it would be inaccurate to say that impecuniosity is keeping them from court.

Members of a class in group proceedings

In Australia, class actions are a large market for litigation investment. Most Australian class actions are filed in the Federal Court,⁸⁹ Federal Court class actions are referred to in this thesis as 'Part IV actions'.⁹⁰ Between 2013 and 2018, 64% of Federal class

⁸⁷ Burford 'Portfolio Financing for In-House Legal Departments' (n 85); see also the hypothetical example at Burford, 'Litigation finance and private equity: A tool to unlock operating value and optimize sales' (28 August 2018) <<http://www.burfordcapital.com/blog/litigation-finance-private-equity/>> accessed 6 May 2019.

⁸⁸ Burford, 'Using Litigation Finance: 12 Leading Lawyers Weigh In (Part II)' (25 October 2017) <<http://www.burfordcapital.com/blog/leading-lawyers-discuss-litigation-finance-2/>> accessed 6 May 2019.

⁸⁹ Allens Linklaters, 'Class Actions: A Ten Year Survey' (2015) <<https://www.allens.com.au/insights-news/insights/2015/05/class-actions-a-ten-year-survey/>> accessed 16 July 2019, 2. Federal Court class actions were 90% of all class actions in 2005-9, and 70% in 2010-14. There are also class action regimes in Victoria, New South Wales, and Queensland.

⁹⁰ Owing to the fact that they were created by Part IV of the Federal Court Act 1976 (Cth).

actions were funded.⁹¹ The proportion of Federal class actions which are funded has increased over time.⁹² In 2017-18, more than 75% of filed proceedings were funded.⁹³

Funding has been critical to the viability of Federal class actions. The reason is that the Federal Court Act, which introduced class actions, failed adequately to deal with the question of costs, creating a regime in which the representative claimant was, prima facie, responsible for costs and adverse costs, and containing no provision for the distribution of costs or adverse costs amongst class members.⁹⁴

The use of funding is particularly frequent in shareholder and investor claims.⁹⁵ In the period March 2013 – March 2018, all of the shareholder claims, and 65% of the investor claims, were funded.⁹⁶ In this period, shareholder and investor claims were the largest categories of claim – 34% and 24% respectively.⁹⁷ Claimants are diverse, ranging from small ‘mum and dad’ investors, to institutional investors, such as local government authorities and pension (superannuation) funds.

⁹¹ Australian Law Reform Commission, *Integrity, Fairness and Efficiency—An Inquiry into Class Action Proceedings and Third-Party Litigation Funders (ALRC Report 134)* (2018), [3.1].

⁹² *ibid* [3.19] and Table 3.2. In the period 1992-2013, it had been 15%. In 2015, Allens Linklaters reported that of class actions filed in Australia (across all jurisdiction), 20% of claims were publicly identified as having been funded in the period 2005-9. By 2010-14, this had risen to 35%: Allens Linklaters (n 89) 3.

⁹³ Australian Law Reform Commission (n 91) [3.18].

⁹⁴ Vince Morabito, ‘Federal Class Actions, Contingency Fees, and the Rules Governing Litigation Costs’ (1995) 21 *Monash University Law Review*, 232-4.

⁹⁵ The distinction between ‘shareholder’ and ‘investor’ claims is not defined in the report, nor in the source materials. However, a review of the tables detailing the underlying claims indicates that shareholder claims include claims made qua shareholder (such as for breach of continuous disclosure obligations), and investor claims are those which relate to other forms of investment (such as claims against rating agencies from investors who have lost money investing in rated investments, or by investors in managed investment schemes).

⁹⁶ Australian Law Reform Commission (n 91) Table 3.3. Consumer protection (12%, of which 31% funded), product liability (7%, of which 50% funded), and mass tort claims (7%, of which 38% funded) were the next largest categories.

⁹⁷ The high instance of shareholder class actions is, in part, a function of unusual features of the substantive law concerning continuous disclosure and misleading and deceptive conduct: Australian Law Reform Commission (n 91) [1.11], [2.68]-[2.75] and Chapter 9.

Collective proceedings in England are far less advanced than in Australia. But this is a developing area of law and practice, which is likely to be a fertile ground for funders in future. There are two main forms of collective proceedings: group litigation orders (GLOs) and collective proceedings in the Competition Appeal Tribunal (CAT).

First, although GLOs have been little-used since their introduction in 2000, there have been several recent examples of high-profile GLO cases having been funded. GLOs were made in the RBS Rights Issue litigation and the Lloyds/HBOS litigation in respect of shareholder claims concerning regulatory breaches – a departure from the personal injury and employment claims which had been the typical subject of previous GLOs.⁹⁸ This has coincided with increased interest in group actions by institutional investors,⁹⁹ who are important participants in Australian class actions. In 2018, a GLO was made in respect of claims against Volkswagen by vehicle owners concerning the diesel emissions scandal.¹⁰⁰ The action involves more than 60,000 claimants.¹⁰¹ All of these high-profile GLOs were funded.¹⁰²

⁹⁸ ‘Group Litigation Orders’ (*HM Courts & Tribunals Service*, 22 May 2018) <<https://www.gov.uk/guidance/group-litigation-orders#list-of-all-group-litigation-orders>> accessed 21 May 2019.

⁹⁹ Woodsford Litigation Funding, ‘The Future of Group Actions and Third Party Funding’ (March 2019) <https://woodsfordlitigationfunding.com/wp-content/uploads/2019/03/The-Future-of-Group-Actions-and-Third-Party-Funding_FINAL.pdf> accessed 17 May 2019, 2.

¹⁰⁰ Details about the claim are available at a dedicated website: ‘VW Emissions Action’ (*Slater & Gordon*) <<https://www.vwemissionsaction.com/>> accessed 21 May 2019.

¹⁰¹ Jamie Maples, Hayley Lund and Sarah Chaplin, ‘United Kingdom’ in Jonathan Polkes and David Lender (eds), *Class Actions 2019 - Getting the Deal Through* (Law Business Research 2018).

¹⁰² The Lloyds/HBOS litigation was funded by Therium: Therium, ‘The Brief, Issue 1’ (February 2016) <https://www.therium.com/thebrief_newsletter/litigation-funding-insights-issue-one/> accessed 10 May 2019; the VW emissions litigation is funded by Therium: Therium, ‘The Brief, Issue 4’ (May 2018) <https://www.therium.com/thebrief_newsletter/may-2018/> accessed 10 May 2019; and the RBS litigation was also funded: *In re RBS Rights Issue Litigation* [2017] EWHC 1217 (Ch); [2017] 1 WLR 4635, [1]-[2]. The latter GLO was initially funded by Vannin, which terminated the funding agreement: *Vannin Capital PCC v RBOS Shareholders Action Group Ltd* [2018] EWHC 2821 (Ch).

Secondly, since 1 October 2015, the Competition Act 1998 has provided for a collective procedure in respect of claims for loss caused by anti-competitive conduct.¹⁰³ Such claims are in the exclusive jurisdiction of the Competition Appeal Tribunal (CAT).¹⁰⁴ Contingency fees are not permitted for these collective proceedings, but third party funding is.¹⁰⁵ They must, however, be the subject of a Collective Proceeding Order (CPO) – a certification process. As of March 2019, the CAT has heard only two applications for a CPO,¹⁰⁶ and neither was successful at first instance. However, the second such application – *Merricks v Mastercard*¹⁰⁷ – has been the subject of a successful appeal. Both the CAT and the Court of Appeal made comments concerning the interpretation of the Competition Act 1998 which were favourable to funders, and confirmed the availability and desirability of commercial funding to facilitate CPO proceedings.¹⁰⁸

It is fair to say that group litigation in England is in a nascent stage. Nevertheless, group litigation is regarded as a fertile ground for future litigation funding investment.

Portfolio funding

Portfolio funding entails a funder providing capital to a claimant who has a group of claims. The claims may be unrelated, and include defence matters. The capital advanced by the funder may be used to pay legal fees and/or simply as operating capital

¹⁰³ See generally Rachael Mulheron, ‘The United Kingdom’s New Opt-out Class Action’ (2017) 37 *Oxford Journal of Legal Studies* 814 as to the history of the procedure.

¹⁰⁴ *ibid* 817.

¹⁰⁵ Rachael Mulheron, ‘The Mere Mirage of a Class Action? A Challenge to *Merricks v Mastercard Inc*’ (2018) 37 *Civil Justice Quarterly* 216, 216 and especially footnote 2.

¹⁰⁶ *Woodsford Litigation Funding* (n 99) 5.

¹⁰⁷ *Merricks v Mastercard Incorporated* [2017] CAT 16.

¹⁰⁸ *ibid* [127]; *Merricks v MasterCard Incorporated* [2019] EWCA Civ 674, [60].

for the claimant's business.¹⁰⁹ Portfolio finance is usually provided on a non-recourse basis, so the funder only gets its investment back – and a profit – from any proceeds of the claims.¹¹⁰ Because of the diversification of risk across the portfolio, the cost to the claimant (i.e. the funder's percentage return) is likely to be less than for single case funding.¹¹¹

Portfolio funding is a growing area of practice.¹¹² The claimant will be a party with numerous claims – for example, a company with several claims.¹¹³ It may also be useful where a claimant has several small claims, each of which is individually too small for single-case funding – for example, insolvency practitioners.¹¹⁴ Portfolio financing has the same budget benefits of single-case funding – that is, it removes legal expenses from a company's balance sheet, and removes risk.¹¹⁵

Another form of portfolio finance is with the clients of a particular client. By way of example, in July 2019 the litigation funder Augusta announced a £25 million portfolio agreement with Pinsent Masons, a firm of solicitors. This agreement was said to provide clients with 'the benefit of a dedicated facility at preferred rates, including a fast-tracked due diligence process and transparent commercial terms'.¹¹⁶ A representative of Pinsent Masons said of the agreement:

I believe our arrangement with Augusta will provide Third Party Funding to our clients efficiently, quickly, on clear terms and at lower

¹⁰⁹ Burford, '5 Minutes On... Portfolio Finance' (17 April 2019) <<http://www.burfordcapital.com/blog/5-minutes-on-portfolio-finance/>> accessed 5 May 2019.

¹¹⁰ *ibid.*

¹¹¹ *ibid.*

¹¹² *ibid.*

¹¹³ Rowles-Davies (n 3) [3.83]-[3.84].

¹¹⁴ *ibid* [3.85].

¹¹⁵ Burford, '5 Minutes On... Portfolio Finance' (n 109).

¹¹⁶ John Freund, 'Pinsent Masons Agrees to £25M Litigation Funding Facility with Augusta' (*Litigation Funding Journal*, 4 July 2019) accessed 5 July 2019.

cost. We've been able to negotiate considerably better terms than our clients would typically receive from Funders if we or they made an individual approach to the market.

The fast-tracked due diligence process entails that claims which are suitable for funding are reviewed by 'a joint committee from Pinsent Masons and Augusta'.

Portfolio financing agreements in this form might create the potential for novel ethical questions to arise – for example, who will the solicitor act for if there is a dispute between funder and claimant? The particular issues raised by portfolio agreements are outside the scope of this thesis.

Law firm finance

A new form of funding emerging in England is for funders to advance funds to a law firm. The funds are used to enable the firm to offer alternative fee structures.¹¹⁷ It works in the following way. If a firm wishes to offer conditional fee agreements, or damages-based agreements ('DBAs') (together, 'alternative fee structures') to its clients, then the firm (1) will not be paid until the litigation bears fruit, in the form of a judgment or settlement, and (2) takes a risk that it will not be paid if the litigation is unsuccessful. Either a firm must carry the work-in-progress and disbursements, or must take on bank borrowing. Either route entails obvious risks to the firm. These economic considerations will constrain the ability of any firm to offer alternative fee structures.

A funder may advance capital to the firm on a non-recourse basis, and then share in the law firm's returns in the event of success. The firm is therefore able to increase the volume of work that it performs using alternative fee structures¹¹⁸. The funder

¹¹⁷ Rowles-Davies (n 3) [3.75]-[3.82].

¹¹⁸ Burford, 'Relieve Fee Pressures—and Keep Clients Happy—with Legal Finance' (9 October 2018) <<http://www.burfordcapital.com/blog/relieve-fee-pressures-keep-clients-happy-with-legal-finance/>> accessed 6 May 2019; *ibid* [3.82].

might be paid an annual interest rate on the funds advanced, or share a percentage of the uplift on a CFA, or share in the firm's recoveries under DBAs.¹¹⁹

Law firm financing may also take the form of 'fee acceleration', in which a firm effectively sells its outstanding bills to a funder, at a discount.¹²⁰

Law firm financing has been most prevalent in the United States. But in 2017, Burford became the first major funder to enter a portfolio agreement with a UK law firm, Shepherd and Wedderburn.¹²¹ Burford provided several million pounds in capital to the firm to enable it to grow its use of alternative fee arrangements.¹²² In exchange, Burford will receive a share of the proceeds of successful matters.¹²³ Shepherd and Wedderburn reported that their clients – mid-sized corporates – found DBAs appealing, but the firm did not wish to take on bank borrowing, or carry large amounts of work-in-progress and disbursements.¹²⁴

The use of a funding model in which a solicitor works on a DBA, but also enters into a funding agreement with a third-party funder, appears to have evolved (at least in part) in response to perceived difficulties in the DBA regime.¹²⁵ Specifically, it was

¹¹⁹ Rowles-Davies (n 3) [3.78]-[3.82].

¹²⁰ Burford, 'Legal Finance: The Year-End Financial Tool Law Firms Need' (30 October 2018) <<http://www.burfordcapital.com/blog/year-end-law-firm-financial-tool/>> accessed 6 May 2019.

¹²¹ Burford, 'Shepherd and Wedderburn's Guy Harvey Discusses Law Firm Portfolio Finance—and What it Means for the Industry' (13 March 2018) <<http://www.burfordcapital.com/blog/shepherd-wedderburns-guy-harvey-discusses-law-firm-portfolio-finance-means-industry/>> accessed 6 May 2019.

¹²² Burford, 'Shepherd and Wedderburn Invests in Growth with Innovative Portfolio Financing from Burford Capital' <<http://www.burfordcapital.com/newsroom/shepherd-wedderburn-invests-growth-innovative-portfolio-financing-burford-capital/>> accessed 6 May 2019.

¹²³ *ibid.*

¹²⁴ Burford, 'Shepherd and Wedderburn's Guy Harvey Discusses Law Firm Portfolio Finance—and What it Means for the Industry' (n 121).

¹²⁵ See generally Civil Justice Council, *The Damages-Based Agreements Reform Project: Drafting and Policy Issues* (August 2015), section 9; see also Rachael Mulheron and Nicholas Bacon, *The 2019 DBA Reform Project: Explanatory Memorandum* (October 2019), 14-15.

generally understood that the Damages-Based Agreements Regulations 2013 did *not* permit the use of a hybrid DBA (that is, an agreement in which a solicitor charges a low hourly rate for the duration of the litigation, and *also* receives a share of the claimant’s recovery in the event of success).¹²⁶ This is because (in simplified terms) those Regulations preclude any provision in a DBA that requires the solicitor’s client to pay an amount other than the percentage success fee.¹²⁷ However, the Court of Appeal has recently held that the Regulations apply only to the part of the retainer that deals with the solicitor’s share of recoveries – and do *not* restrict the other provisions that may be included in a retainer, such as provision for other payments to be made on a different basis.¹²⁸ Thus, hybrid DBAs appear to be permissible under the existing Regulations. It may be, therefore, that there is a diminished need for the ancillary use of third-party funding by solicitors in support of DBAs.¹²⁹

Law firm financing raises unique policy issues and risks. Existing literature on funding assumes that there is at least some degree of separation between funder and solicitor, and even that funder and claimant might share interests – for example in minimising legal costs – which might be opposed to the solicitor’s interests. Where law firm financing is used, the interests of the funder and solicitor are more likely to be aligned. For this reason, law firm financing is outside the scope of this thesis.

¹²⁶ Peter Hurst, Simon Middleton and Roger Mallalieu, *Costs & Funding following the Civil Justice Reforms: Questions & Answers* (6th edn, Sweet and Maxwell 2020) [2.26].

¹²⁷ Damages-Based Agreements Regulations 2013/609, paragraph 4(1) and see also the definition of ‘payment’ at paragraph 1(2).

¹²⁸ *Zuberi v Lexlaw Limited* [2021] EWCA Civ 16, [33]-[34] (and see also [35]-[43]) (Lewison LJ); [77] (Coulson LJ); see also [64] (Newey LJ) – his Lordship disagreed with the analysis, but aptly summarised the effect of the majority’s reasoning.

¹²⁹ It should be noted that in 2019, Professor Rachael Mulheron and Nicholas Bacon QC had proposed amendments to the Damages-Based Agreements Regulations 2013 that included express provision for hybrid DBAs, in part to ‘circumvent the need for solicitors to enter into “side agreements” with third party funders’: see Mulheron and Bacon (n 125) 15.

Defence funding

It is possible for a defendant to enter a litigation funding agreement. It may work in the following way. The funder provides funds to be put towards the defence, on a non-recourse basis.¹³⁰ These funds, and any profit, are returned to the funder only on the occurrence of some ‘success’ criterion, for example, based on the savings made by the defendant in having to pay less than the claimed amount, or succeeding in having the claim struck out.¹³¹ The use of litigation funding serves to mitigate the risk of loss, and ensures that any costs to the defendant are predictable.¹³² It is also possible to fund a defence where it is linked to a strong counterclaim, or as part of a portfolio with claims in which the client is a claimant.¹³³

Defence financing of a single matter is rare, because there is no pool of funds from which the funder’s success fee can be drawn. But it might be apt in some cases – for example, where a defendant company is well-capitalised so that it can pay the funder’s fees from its own resources in the event of success.¹³⁴ Alternatively, it might be used where a large sum has been paid into court, or is subject to a freezing order, so that the defendant will effectively receive some funds if it is successful.¹³⁵

In this thesis, the term ‘claimant’ is used, for convenience, to describe the litigant who uses funding. But occasionally a defendant might be funded.

¹³⁰ Burford, ‘Financing Litigation Defense: How it Works’ (7 March 2019) <<http://www.burfordcapital.com/blog/financing-litigation-defense-how-it-works/>> accessed 5 May 2019.

¹³¹ Rowles-Davies (n 3) [3.24]-[3.28].

¹³² Burford, Financing Litigation Defense: How it Works (n 130). See generally the worked example at *ibid* [3.25]-[3.31].

¹³³ Burford, Financing Litigation Defense: How it Works (n 130).

¹³⁴ Rowles-Davies (n 3) [3.31].

¹³⁵ *ibid* [3.25].

Growth of the litigation funding market

It is fair to say that the litigation funding market has grown exponentially in recent years.¹³⁶ Taking Australia as an example, in 2014, it was estimated that IMF Bentham (now Omni Bridgeway) had 69% market share,¹³⁷ and in the period 2010-14 had funded 54% of funded class actions (across all jurisdictions).¹³⁸ But by December 2018, the ALRC reported that there were 33 funders operating in the Australian market, stating that this ‘lack of homogeneity’ presented a difficulty in regulating.¹³⁹ Of the nine current funder members of the English Association of Litigation Funders, six were founded in 2009 or later.

Litigation funders report that the development of the various litigation funding markets has been in response to market demand. That is, new forms of finance have emerged in response to market demand. Worldwide, several factors have been suggested as driving increased demand, including the increased use of funding for balance sheet purposes, or by companies who do not wish to divert funds from their central business.¹⁴⁰

On the supply side, there has been an enormous influx of funds invested into the litigation funding market in recent years. The reasons for this appear to be twofold. First, litigation funders report high success rates and good profits.¹⁴¹ Secondly,

¹³⁶ In addition to the statistics cited in the remainder of the paragraph, see also Jason Geisker and Jenny Tallis, ‘Australia’ in Leslie Perrin (ed), *The Third Party Litigation Funding Law Review* (Law Business Research Ltd 2018), 1-2.

¹³⁷ Saker (n 8) 9.

¹³⁸ Allens Linklaters (n 89) 3.

¹³⁹ Australian Law Reform Commission (n 91) Appendix G and see [2.15], [3.41].

¹⁴⁰ Bench Nieuwveld (n 24) 11.

¹⁴¹ As to financial performance, see Burford, ‘Burford Capital Reports Record 2018 results’ (13 March 2019) <<http://www.burfordcapital.com/newsroom/burford-capital-reports-record-2018-results/>> accessed 6 May 2019. As to IMF, see Saker (n 8) 4; #2930, 11.

litigation funding is an investment which is performed independently of other investments, such as bonds, or the stock market.¹⁴² Thus, it provides a route for investors to obtain returns even if interest rates are low, or the stock market is volatile. This has been particularly desirable in the wake of the GFC.¹⁴³ Investors in litigation funding are diverse – funders range from stock market listed companies to family offices.¹⁴⁴

Related practices

Much of the existing literature on litigation funding emanates from the United States. However, there are radically different practices in the United States funding market. Specifically, the market includes both consumer and commercial litigation investment. As Hensler observes, these have almost nothing in common.¹⁴⁵

The consumer market paradigm is that individual, impecunious claimants receive a cash advance (which might perhaps be used for necessary medical and living expenses as they await judgment). Funds are typically lent on a non-recourse basis, contingent on the success of the litigation. In the event that the litigation is successful, the loan must be repaid at a high rate of interest. In that respect, litigation lending is said by some commentators to share features with the broader category of payday

¹⁴² Rowles-Davies (n 3) [4.33], [4.43], [4.64].

¹⁴³ Bench Nieuwveld (n 24) 11.

¹⁴⁴ See generally Rowles-Davies (n 3) Chapter 4; Bench Nieuwveld (n 24) 75-6.

¹⁴⁵ Deborah R Hensler, 'Third-Party Financing of Class Action Litigation in the United States: Will the Sky Fall?' (2014) 63 DePaul Law Review 1101, 1103.

lending.¹⁴⁶ There is little screening of claims and profits are made by funders because of the sheer volume of work.¹⁴⁷ There is no equivalent practice in England or Australia.

Conversely, in the commercial market, parties engage a lawyer on an hourly fee basis, usually in relation to a larger claim, and the funder pays for the legal costs and disbursements.¹⁴⁸ The larger size of the claims justifies the funder in more careful screening of the merits of individual claims.¹⁴⁹ The commercial market is more similar to the English and Australian markets.

Much of the existing US literature addresses the practice of litigation lending, or treats litigation funding as a practice which includes both the US practice of consumer lending and litigation funding in the sense practised in England and Australia (and used in this thesis).¹⁵⁰ However, owing to the differences in the practices, this literature is not always apposite to the state of the market in England and Australia.

Conclusion

In this chapter, I have sketched the state of the various litigation funding markets, and identified some risks and benefits of each. In the next chapter, I consider the place of

¹⁴⁶ See generally, Susan Lorde Martin, 'The Litigation Financing Industry: The Wild West of Finance Should Be Tamed Not Outlawed' (2004) 10 *Fordham Journal of Corporate and Financial Law* 55; Paige Marta Skiba and Jean Xiao, 'Consumer Litigation Funding: Just Another Form of Payday Lending' (2017) 80 *Law and Contemporary Problems* 117.

¹⁴⁷ Hensler (n 145) 1103-4.

¹⁴⁸ *ibid* 1103.

¹⁴⁹ *ibid* 1105.

¹⁵⁰ See, eg, Susan Lorde Martin, 'Litigation Financing: Another Subprime Industry that has a Place in the United States Market' (2008) 53 *Villanova Law Review* 83; General Thurbert Baker, 'Paying to Play: Inside the Ethics and Implications of Third-Party Litigation Funding' (2013) 23 *Widener Law Journal* 229; Ronen Avraham and Abraham Wickelgren, 'Third-Party Litigation Funding - A Signaling Model' (2014) 63 *DePaul Law Review* 233; Radek Goral, 'Justice Dealers: The Ecosystem of American Litigation Finance' (2015) 21 *Stanford Journal of Law, Business and Finance* 98.

litigation funding in the civil justice system, taking into account this diversity of market practice.

CHAPTER 7: LITIGATION FUNDING AS A MARKET RESPONSE TO BARRIERS TO JUSTICE

In Chapter 2, I explained that judicial acceptance of litigation funding, and the attenuation of maintenance and champerty, has been driven by access to justice concerns. Specifically, courts have perceived the benefits of third-party funding to impecunious and class action claimants.

But this approach is problematic. The last chapter demonstrated that the litigation funding market is diverse. Conventional arguments about ‘access to justice’ do not, therefore, explain or justify the full range of litigation funding. It is, therefore, perhaps unsurprising that some critics are sceptical about the ‘access to justice’ benefits of funding.

In this chapter, I propose a more accurate account of the role of litigation funding in the civil justice system. I explain that the ‘access to justice’ benefits of funding are, in fact, more extensive than conventional arguments suggest.

Freedom of contract

In Chapters 3 and 4, I concluded that there are no reasons of principle why the modern civil justice system ought to express any diffidence towards litigation funding. I suggested that, in fact, litigation funding is entirely consistent with the values of the modern civil justice system.

The starting point for the rest of the thesis, therefore, is that litigants ought to be able to contract for funding for litigation as they choose. This follows simply from the principle of freedom of contract.¹

Of course, where market failures exist, regulation might be necessary – for example, to protect vulnerable parties from entering contracts on disadvantageous terms. Market failures and how they might be regulated are dealt with in later chapters.

I suggest, however, that litigation funding has the potential to play an important role in the modern civil justice system, such that it ought not merely to be tolerated, but be recognised as having a range of benefits.

The role of litigation funding in promoting access to justice – a more complete account

In the previous chapter, I explained that a diverse range of claimants use funding – from well-resourced corporations to small investors who are class action claimants.

Why is litigation funding appealing to such a wide range of claimants? What role is litigation funding performing in the civil justice system?

There are a variety of weaknesses in the civil justice system, which act as barriers or disincentives to litigation. I suggest that litigation funding is a market device which serves to mitigate some of those weaknesses, so that the barriers or disincentives are less of a hindrance. In this sense, litigation funding has a tendency to encourage litigation which might otherwise not be brought, and thus promotes access to justice.

¹ As to which, see generally HG Beale, *Chitty on Contracts* (33rd edn, Sweet & Maxwell 2018), [1-031]-[1-040].

The barriers to justice which litigation funding addresses may be identified by considering the various markets in litigation funding, and the advantages which litigation funders claim to provide to claimants.

First, litigation funding serves to mitigate the high quantum, and unpredictability of litigation costs. High cost is a potentially impenetrable barrier for the impecunious. But high and unpredictable costs are a deterrent to litigation, even for well-resourced claimants. Thus, even well-resourced claimants use litigation funding as a risk mitigation tool.

Secondly, litigation funders can provide assistance in the conduct of litigation. Two important areas are in assisting in strategy, and in reviewing and sense-testing solicitors' bills. There are two reasons why such assistance may be necessary. First, litigation is inherently complex, and even sophisticated claimants may benefit from the advice and assistance of a repeat player. Litigation diverts attention from the central business activities of sophisticated claimants. Why can this not be provided exclusively by the lawyer? Litigation strategy involves questions of commerciality, as well as legal principle. It may be valuable to have advice from a third party who is experienced in litigation, and shares the same interest in the litigation as the claimant.

In respect of solicitors' fees, there is always a potential conflict of interest when a solicitor charges on an hourly basis:² a solicitor has an economic interest in increasing the number of hours billed, and 'it is in the nature of things that economic activity should... follow the most rewarding path'.³ The client's natural inclination to resist

² Kevin M Clermont and John D Currihan, 'Improving on the Contingent Fee' (1978) 63 Cornell Law Review 529; A Mitchell Polinsky and Daniel L Rubinfeld, 'Aligning the Interests of Lawyers and Clients' (2003) 5 American Law and Economics Review 165, 165.

³ AAS Zuckerman, 'A Reform of Civil Procedure - Rationing Procedure rather than Access to Justice' (1995) 22 Journal of Law and Society 155, 163.

high fees is tempered by the indemnity rule.⁴ It is also tempered by the very nature of legal services. Legal services are ‘credence goods’ in economic terms (meaning that the quality cannot easily be assessed even after the event), and the lawyer both identifies the need for service and performs the resulting work, which creates ‘supplier-induced demand’, with a tendency to drive up cost – problems which arise largely because of the information asymmetry between lawyer and client, and are mitigated by the client’s experience and knowledge.⁵ Funders are well-placed to mitigate these problems. As repeat players in the market for litigation services, they have knowledge and experience, and are able to exert commercial pressure on solicitors to revise fees downwards. Funders report applying anxious scrutiny to solicitors’ bills.⁶ This is discussed further in Chapter 11.

Thirdly, litigation funding in the class action context mitigates the practical difficulties with commencing and prosecuting a claim. Litigation funders can (and do) investigate claims, coordinate the class and instigate the action, acting as prime movers to start proceedings. Facilitating class actions creates further benefits: it reduces the risk that there will be a disproportionality between the cost of proceedings and the likely recovery. Disproportionate costs create a barrier to justice even for the well-resourced. Paying disproportionately high costs (and risking disproportionately high adverse costs) is irrational, irrespective of means.⁷

⁴ *ibid.*

⁵ The market failures of the legal services market are well-documented, and are summarised in Frank H Stephen, *Lawyers, Markets and Regulation* (Edward Elgar 2013), 12-16.

⁶ Vicki Waye, ‘The Initiation and Operations Phase of the Litigation Funder - Class Action Law Firm Relationship: an Australian Perspective’ (2018) 60 *International Journal of Law and Management* 595, 610.

⁷ Lord Justice Briggs, *Civil Courts Structure Review: Interim Report* (2016), [5.40].

The access to justice benefits of litigation funding can therefore be summarised

as:

- Mitigating the effect of high and unpredictable litigation costs – an impervious barrier for the impecunious, but a deterrent to any rational litigant;
- Enabling litigation to proceed where the cost of a single claim is disproportionate to the quantum (class actions);
- Mitigating class coordination problems in class actions (including how costs are to be distributed amongst the class);
- Reducing the effects of the complexity of the litigation process;
- Mitigating conflicts of interest between lawyer and client in respect of hourly rate billing (through the status of the funder as an experienced, repeat player, who has the necessary expertise to scrutinise bills and can exert commercial pressure on solicitors).

We can therefore identify the corresponding barriers as being:

- The high cost of litigation (that is, the high cost of litigation in absolute terms);
- The inherent difficulties in crafting an effective and fair class action regime;
- The high cost of litigation relative to the amount claimed;
- The unpredictability of litigation costs;
- The difficulty and complexity of litigation
- The inherent conflict of interest which exists between lawyer and client when a lawyer is retained on an hourly rate basis.

Therefore, when we consider the place of litigation funding in the civil justice system, we need to have a broader sense of what are the barriers, and the ways in which litigation funding mitigates these.

In all circumstances in which it is used, litigation funding has a tendency to increase the prospect of a claim being brought. It does so by mitigating the hurdles listed above. In some cases – it is impossible to know how many – this assistance means the difference between litigating, and not litigating. It is in this broad sense that litigation funding promotes access to justice.

The right of access to justice

The right of access to justice is well-recognised in England and Australia.⁸ In England, the right of access to justice has been described as being constitutional in nature, with the result that it can be abrogated only by express legislative provision.⁹ Even in Australia (where the Constitution makes no express reference to a right to access the court), the common law right of access to court has been described as ‘deeply rooted in constitutional principle’.¹⁰

In England, the right of access to justice has received consideration in light of the obligations imposed by Article 6 of the European Convention on Human Rights (‘the ECHR’). Specifically, access to justice is an aspect of the right to a fair trial which

⁸ *Bremer Vulkan Schiffbau und Maschinenfabrik v South India Shipping Corporation Ltd* [1981] AC 909 (HL), 977; *Raymond v Honey* [1983] 1 AC 1 (HL), 13; *R v Secretary of State for the Home Department; Ex parte Leech (No 2)* [1994] QB 198; *R v Lord Chancellor, ex p Witham* [1998] QB 575; *Unity Insurance Brokers Pty Ltd v Rocco Pezzano Pty Ltd* (1998) 192 CLR 602, [55] (Gummow J); *Momcilovic v R* [2011] HCA 34 ; (2011) 245 CLR 1, [444] (Heydon J);

⁹ *Ex parte Witham* (n 8) 581, 585.

¹⁰ *Unity Insurance Brokers* (n 8) [55] (Gummow J). See also Steven Rares, ‘Is Access to Justice a Right or a Service?’ (Access to Justice - Taking the Next Steps Symposium, Monash University, Melbourne, 26 June 2015), [19], who describes access to a court as a ‘fundamental common law right’, and see also [30].

is guaranteed by Article 6.¹¹ It has been observed that the ECHR did little to alter the common law in this respect.¹² However, as observed in Chapter 3, the increase in rights discourse in recent years has led to an increased focus on rights, including the right of access to justice.

It is well-recognised that high fees pose a barrier to justice. In England, the jurisprudence on the question of fees or costs and access to justice has been addressed in three broad circumstances: (1) the legitimacy of the CFA regime which existed in England and Wales between 1999 and 2013 ('pre-LASPO CFAs'),¹³ (2) whether there is an obligation on the state to provide civil legal aid, and (3) whether there are limits on the level of fees which may be imposed.

The problems with pre-LASPO CFAs – the perverse incentives they created, and the barriers to justice which they imposed on defendants – are well-documented,¹⁴ and it is outside the scope of this thesis to detail these. In *MGN v UK*,¹⁵ the European Court of Human Rights found that the use of a pre-LASPO CFA to fund litigation against a newspaper was inconsistent with Article 10 of the ECHR (protecting the right to freedom of speech). It was disproportionate to require the defendant to pay high success fees, purportedly in the interests of access to justice, in circumstances where the claimant was 'wealthy and not in the category of persons considered excluded from

¹¹ *Golder v UK* [1975] ECHR 1; Jeremy McBride, 'Access to Justice and Human Rights Treaties' (1998) 17 *Civil Justice Quarterly* 235, 236-7.

¹² *R v Secretary of State for the Home Department, ex p Simms* [2000] 2 AC 115, 131-2.

¹³ The CFA regime was introduced in 1999 via the Access to Justice Act 1999 (UK), and substantially amended from April 2013 onwards by the Legal Aid, Sentencing and Punishment of Offenders (LASPO) Act 2012 (UK).

¹⁴ For a detailed treatment, see John Peysner, *Access to Justice: A Critical Analysis of Recoverable Conditional Fees and No Win No Fee Funding* (Palgrave Macmillan 2014). See also Adrian Zuckerman, *Zuckerman on Civil Procedure: Principles of Practice* (3rd edn, Thomson Reuters, Sweet & Maxwell 2013), [27.201]-[27.208], [27.229]-[27.236].

¹⁵ *MGN Ltd v UK* Case Reference Application No 39401/04, [2011] ECHR 66, especially [218]-[220].

access to justice for financial reasons’. The reference to access to justice *for financial reasons* recognises, implicitly, that financial reasons are not the only barrier to justice.

In England, the right of access to justice may provide an obligation on the state to provide civil legal aid. The question whether to fund representation is one for the Legal Services Commission,¹⁶ although an indication from the court that a case requires representation is likely to be influential.¹⁷ The test for whether legal aid is required by Art 6 is:¹⁸

whether a court is put in a position that it really cannot do justice in the case because it has no confidence in its ability to grasp the facts and principles of the matter on which it has to decide. ... It is not sufficient that the court might feel that the case could be presented better; the question for the court is whether it feels that the case is being, or will be, presented in such a way that it cannot do what it is required to do — that is to say, reach a just decision.

In a similar vein, the European Court of Human Rights has stated that the state is obliged to provide civil legal aid where it is necessary to enable the litigant ‘to present [their] case properly and satisfactorily’.¹⁹

There is no equivalent right in Australia in civil proceedings.²⁰

As to the imposition of fees, in the leading case of *Ex parte Witham*, a legislative order which imposed court fees indiscriminately on all litigants, with no exemption for those who could not afford them was – in the absence of an express legislative provision enabling the abrogation of the right of access to the court – was held to be unlawful.²¹

¹⁶ *Re Perotti* [2003] EWCA Civ 1521, [23]-[24].

¹⁷ *ibid* [26].

¹⁸ *ibid* [32].

¹⁹ *Airey v Republic of Ireland* (1979) 2 EHRR 305, [24], [26].

²⁰ *New South Wales v Canellis* (1994) 181 CLR 309, 328 (Mason CJ, Dawson, Toohey and McHugh JJ).

²¹ *Ex parte Witham* (n 8).

In *R (UNISON)*, employment tribunal fees were imposed unlawfully in circumstances where remissions were only available in relatively limited circumstances, and were unaffordable to people of apparently ordinary income and means.²² It was also relevant there that employment claims are generally small in quantum, such that the fee was disproportionate to likely recovery and made it ‘futile or irrational to bring a claim’.²³

If court fees obstruct access to justice, then so too must high legal costs – both may present an insuperable hurdle for the impecunious, and a deterrent for other litigants.

The concept of access to justice is most commonly associated with issues of affordability. But even the (relatively limited) Article 6 jurisprudence on the right of access to justice recognises that there are a variety of potential obstructions to justice. An emerging body of law indicates that access to justice is not solely about the barriers imposed by high costs. It is recognised, for example, that exposure to the risk of adverse costs may deter litigation;²⁴ and that an unduly complex legal process may also infringe the right of access to justice.²⁵

Thus, we can see emerging recognition that access to justice is not just about the impecunious. A wider range of barriers exist, and may ground access to justice considerations.

²² *R (UNISON) v Lord Chancellor (Equality and Human Rights Commission and another intervening) (Nos 1 and 2)* [2017] UKSC 51; [2017] 3 WLR 4. As to the threshold of affordability, see further below.

²³ *ibid* [96].

²⁴ McBride (n 11) 263.

²⁵ *ibid* 266.

Further, the principle of access to justice also informs a diverse range of other rights. It finds expression in a variety of principles.²⁶ For example, where legislation purports to restrict access to courts, it is presumed that parliament ‘does not intend to cut down the jurisdiction of the courts save to the extent that the legislation in question expressly so states or necessarily implies’.²⁷ Another example is the approach of the court to vexatious litigants: the threshold for making a civil restraint order under the English CPR is high,²⁸ and in Australia, even where a person has engaged in repeated vexatious litigation, the court will be slow to exercise its powers to restrain them from future litigation because of the fundamental importance of access to justice.²⁹ A further example may be seen in the context of applications for security for costs. In Australia, where a claimant who is a natural person is impecunious, the court will not award security for costs in favour of the defendant (save in certain very limited circumstances) because of the importance of ensuring that the claimant has access to the court, even though the consequence is that the defendant must accept the risk that its costs will not be paid in the event it successfully defends the claim.³⁰ Similarly, in England, a ‘prime consideration’ in the decision whether to order security is whether the order will deprive the claimant of their right to access the court.³¹

²⁶ The following paragraph is adapted from Adrian Zuckerman and others, *Zuckerman on Australian Civil Procedure* (LexisNexis Butterworths 2018), [3.111], which was written by the author.

²⁷ *Plaintiff S157/2002 v Commonwealth* [2003] HCA 2; (2003) 211 CLR 476, [72] (Gaudron, McHugh, Gummow, Kirby and Hayne JJ). See also *Anisminic Ltd v Foreign Compensation Commission* [1969] 2 AC 147 (HL), 170 (Lord Reid).

²⁸ *Sartipy v Tigris Industries Inc* [2019] EWCA Civ 225; [2019] 1 WLR 5892, [25]-[37].

²⁹ *Kowalski v MMAL Staff Superannuation Fund Pty Ltd ACN 064 829 616* [2007] FCA 1069; (2007) 242 ALR 370, [44] (Finn J).

³⁰ *Harpur v Ariadne Australia Ltd* [1984] 2 Qd R 523, 530 (Connolly J); *Lee v Abedian* [2017] QSC 22, [36]-[37] (Applegarth J). Different considerations apply where the claimant is a corporate entity.

³¹ *Olatawura v Abiloye* [2002] EWCA Civ 998; [2003] 1 WLR 275, [22].

Solutions to the high and unpredictable cost of litigation: a diverse and growing landscape

Having identified earlier in the chapter the various barriers to justice which litigation funding mitigates, we can see that litigation funding is but one solution in a growing landscape of market and regulatory responses. It is beyond the scope of this thesis to explore the reasons for high and unpredictable costs, but likely causes include hourly-based billing, complexity of litigation, and cost-shifting.³²

Other solutions to the problems of high and unpredictable costs are possible, and indeed there are numerous recent amendments to the rules, and proposals for further amendments, which are intended to alleviate either cost or unpredictability of cost, particularly in England. All of the proposals and reforms identified below have been made in England, unless otherwise indicated.

First, there are reforms which directly reduce quantum or uncertainty of costs.

These include:

- Only proportionate costs may be awarded on assessment.³³
- Forward-looking costs management – including the use of budgets – is mandatory for most claims with a value between £25,000 and £10 million.³⁴

³² Lord Justice Rupert Jackson, ‘Fixed Costs - The Time has Come’ (IPA Annual Lecture, 28 January 2016), [2.2].

³³ CPR 44; see Lord Justice Rupert Jackson, *Review of Civil Litigation Costs: Final Report* (2009), chapter 3, [5.15]-[5.23].

³⁴ CPR r 3.12 to 3.18 inclusive. Lord Justice Rupert Jackson, ‘Confronting Costs Management’ (Harbour Lecture, 13 May 2015), [2.1]-[2.18].

- Fixed costs are imposed in certain categories of claim,³⁵ and there are proposals to expand the circumstances in which they are available.³⁶ Fixed costs are available in limited circumstances in Australia.³⁷
- Cost capping orders are available in England,³⁸ and in some Australian jurisdictions.

Secondly, there are reforms which reduce the need for lawyers' services. These include:

- Expanding the small claims jurisdiction, by increasing the value of claims which must be heard in that jurisdiction.
- Creating an online court,³⁹ the benefits of which are said to be the ease of such a system for a litigant in person, reduction in delay, and improved affordability.⁴⁰

³⁵ *Zuckerman on Civil Procedure* (n 14) [27.192]-[27.199].

³⁶ Jackson, *Review of Civil Litigation Costs: Final Report* (n 33) chapters 15 and 16; Lord Justice Rupert Jackson, *Review of Civil Litigation Costs: Supplemental Report Fixed Recoverable Costs* (2017), Chapter 11, [2.1]-[2.2]; Ministry of Justice, *Extending Fixed Recoverable Costs in Civil Cases: Implementing Sir Rupert Jackson's Proposals* (2019), [1.5]-[1.7]. See generally Rupert Jackson, 'Controlling Recoverable Costs' in Rabeea Assy and Andrew Higgins (eds), *Principles, Procedure, and Justice: Essays in honour of Adrian Zuckerman* (Oxford University Press 2020) for an overview of the current position.

³⁷ *Zuckerman on Australian Civil Procedure* (n 26) [28.179].

³⁸ Although see Jackson, 'Confronting Costs Management' (n 34) 24.

³⁹ Civil Justice Council - Online Dispute Resolution Advisory Group, *Online Dispute Resolution for Low Value Civil Claims* (2015), especially [1.8]-[1.11] and 'Recommendations', [2.1]-[2.8]; JUSTICE, 'Delivering Justice in an Age of Austerity' (2015) <<https://justice.org.uk/justice-age-austerity-2/>> accessed 13 March 2016, especially [2.17]-[2.20]; Briggs, *Civil Courts Structure Review: Interim Report* (n 7) chapter 6. The concept has been supported by The Rt Hon Sir Ernest Ryder, 'The Modernisation of Access to Justice in Times of Austerity' (5th Annual Ryder Lecture, the University of Bolton, 3 March 2016), [24]-[34]; see also Sir Henry Brooke, 'A Future Online Civil Court: (3) Six Questions to Answer' (24 January 2016) accessed 26 March 2016, but compare 'Bar Council Cautious over Plans to Discard Lawyers' (*Solicitors Journal*, 19 January 2016) <<http://www.solicitorsjournal.com/news/management/technology/25209/bar-council-cautious-over-plans-discard-lawyers>> accessed 16 February 2016. See Michael Briggs, 'The Civil Online Court in England' in Rabeea Assy and Andrew Higgins (eds), *Principles, Procedure, and Justice: Essays in honour of Adrian Zuckerman* (Oxford University Press 2020).

⁴⁰ Civil Justice Council - Online Dispute Resolution Advisory Group (n 39) 'Introduction and overview', [3.2], [3.8], [6.3], [6.4], [9.4].

- Unbundling legal services – that is, retaining solicitors only for discrete steps in legal proceedings.⁴¹ Lawyers act on limited retainers in the England⁴² and Australia,⁴³ although attention on these sorts of arrangements has been relatively recent.
- Offering support for litigants in person – initiatives to achieve this goal can be found in England⁴⁴ and in some Australian jurisdictions.⁴⁵

Thirdly, there are reforms which transfer the costs of litigation to a third party.

These include:

- Contingent legal aid funds (CLAF), which essentially operate in a similar way to litigation funding, but on a not-for-profit basis, with funding available to claimants of limited means, with sufficiently meritorious claims. The Law Society of South Australia operates such a scheme,⁴⁶ and there have been proposals in England for a CLAF.⁴⁷
- After-the-event insurance.

⁴¹ Law Society of England and Wales, ‘Unbundling Legal Services’ (*Law Society of England and Wales*, 19 March 2015) <<http://www.lawsociety.org.uk/support-services/advice/practice-notes/unbundling-civil-legal-services/>> accessed 25 March 2016, ‘2. What is Unbundling?’.

⁴² *ibid.*

⁴³ Australian Government Productivity Commission, *Access to Justice Arrangements (Productivity Commission Inquiry Report No 72)* (2014), section 19.2, 644-52, especially 644.

⁴⁴ HHJ Edward Bailey and others, *A Handbook for Litigants in Person* (2013).

⁴⁵ See, eg, Law Access, ‘About Us’ (*Law Access*) <<http://www.lawaccess.nsw.gov.au/Pages/about-us/about-us.aspx>> accessed 29 March 2016; Law Access, ‘Representing Yourself - LawAssist’ (*Law Access*) <<http://www.lawaccess.nsw.gov.au/Pages/representing/Representing-yourself.aspx>> accessed 29 March 2016.

⁴⁶ Law Society of South Australia, ‘Litigation Assistance Fund (LAF)’ <https://www.lawsocietysa.asn.au/LSSA/Lawyers/Support/Litigation_Assistance_Fund.aspx> accessed 24 March 2016.

⁴⁷ Lord Justice Rupert Jackson, ‘The Case for a CLAF’ (Solicitors’ Costs Conference, 2 February 2016), particularly [1.1] and [4.1]-[4.13].

- Qualified one-way costs shifting in England,⁴⁸ and the provision in Australia by which a small business which commences proceedings in respect of anti-competitive business practices⁴⁹ may apply at any time for an order that it will not be liable for adverse costs in any event.⁵⁰

Finally, there are reforms which permit alternative fee arrangements by lawyers.

These include:

- Conditional fee agreements, which are permitted in England⁵¹ and all Australian jurisdictions.⁵²
- Damages-based agreements, which are permissible in England.

It is beyond the scope of this thesis to explore these other solutions in detail, or to compare their advantages and disadvantages. It is sufficient to note that the high and unpredictable cost of litigation has sparked a variety of solutions and proposed solutions, by rule-makers, governments and the market, of which litigation funding is but one.

The problems with the existing approach to litigation funding and access to justice

Having considered how litigation funding facilitates access to justice – given the barriers which currently exist in the civil justice system – we can now see that conventional arguments concerning the access to justice benefits of litigation funding

⁴⁸ *Zuckerman on Civil Procedure* (n 14) [27.175]-[27.191].

⁴⁹ That is, proceedings under Part IV of the Competition and Consumer Act 2010 (Cth).

⁵⁰ Treasury Laws Amendment (2018 Measures No 5) Act 2019 (Cth), s 7, which amended Competition and Consumer Act 2010 (Cth), s 82.

⁵¹ *Zuckerman on Civil Procedure* (n 14) [27.214]-[27.220].

⁵² *Zuckerman on Australian Civil Procedure* (n 26) [28.189]-[28.193].

(namely, that it enables the impecunious to litigate) are limited. They are an unhelpful way to think about the role of litigation funding in the civil justice system.

Access to justice concerns focus on the impecunious, or class actions

When driven to identify the benefits of litigation funding, it is usual for courts and commentators to refer to the benefits to the impecunious, and class action claimants.

First, it is identified that litigation funding assists impecunious litigants. Thus, it is accepted that litigation funding may enable a party to commence and pursue litigation where they otherwise would have insufficient funds to do so. Into this category may be placed insolvent companies.⁵³

In England and Australia, litigation funding has been recognised as having a particularly important role to play in facilitating class actions.⁵⁴ This has come about differently in each jurisdiction. In England, as explained in Chapter 2, the costs regime in the CAT was drafted with the intention of making collective actions attractive to funders.⁵⁵

Conversely, in Australia, the legislation which created class actions *failed* to deal with costs. It is well-accepted that the high costs – and high risks to the representative claimant of adverse costs – of a class action are a substantial deterrent to

⁵³ Civil Justice Council, *Improved Access to Justice – Funding Options & Proportionate Costs: Report & Recommendations* (2005), [43]; Standing Committee of Attorneys-General, *Litigation Funding in Australia: Discussion Paper* (2006), [2.1]; Civil Justice Council, *Improved Access to Justice* (2007), [127], and see also [154]; Australian Government Productivity Commission (n 43) 607.

⁵⁴ Standing Committee of Attorneys-General (n 53) [2.1]; Civil Justice Council (n 53) [127], and see also [156]; Australian Government Productivity Commission (n 43) 607. As to the role of litigation funding in facilitating class actions, see also Australian Law Reform Commission, *Integrity, Fairness and Efficiency—An Inquiry into Class Action Proceedings and Third-Party Litigation Funders (ALRC Report 134)* (2018), [1.29].

⁵⁵ *Merricks v MasterCard Incorporated* [2019] EWCA Civ 674, [60].

commencing proceedings, and that in mitigating these problems litigation funding ‘has provided a significant means of improving access to justice’.⁵⁶

Thus, put another way, litigation funding is recognised to mitigate just two barriers to justice:

- The high cost of litigation (that is, the high cost of litigation in absolute terms); and
- The high cost of litigation relative to the amount claimed.

It is rare to find any acknowledgement, in case law or commentary, that the modern litigation funding industry has expanded well beyond cases which satisfy this definition of access to justice, or that the benefits of funding extend beyond enabling access for the impecunious or the class action claimant.⁵⁷ A rare exception is the recent report of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration, which observed that:⁵⁸

... much of the focus of the litigation finance market today is on the growing corporate utilization of funding by large, well-resourced entities. These entities may be looking for ways to manage risk, to reduce legal budgets, take the cost of pursuing arbitration off-balance sheet, or to pursue other business priorities instead of allocating resources to financing an arbitration matter. Put simply, funding is not only for those that are impecunious....

⁵⁶ ‘Financing Access to Justice: Third-Party Litigation Funding and Class Actions in Australia’ (2014) 55 Canadian Business Law Journal 17, 18, and see also 25-7; *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148; (2016) 245 FCR 191, [180]-[183], [192].

⁵⁷ *Stiftung Salle Modulable v Butterfield Trust (Bermuda) Ltd* [2014] BMSC 13; [2014] SC (Bda) 14 Com.

⁵⁸ International Council for Commercial Arbitration, *Report of the ICCA-Queen Mary Task Force on Third-Party Funding in International Arbitration* (2018), 20.

Another rare exception is the remarks of French J (as his Honour then was) in *QPSX v Ericsson*, which directed attention to the possibility of litigation funding introducing:⁵⁹

...a welcome element of commercial objectivity into the way in which ... budgets are framed and the efficiency with which the litigation is conducted....

But these remarks have not been picked up or developed in subsequent Australian judgments.

If access to justice is just about aiding the impecunious, who are the impecunious?

A further problem in the conventional approach to litigation funding and access to justice is that it is difficult to know where to draw the line in identifying ‘access to justice’ cases. The problem is well-demonstrated by the Hong Kong case law, where maintenance and champerty are still unlawful, and ‘access to justice’ remains one of the very few exceptions to the prohibition.⁶⁰ The courts have held that the ‘access to justice’ exception is limited to circumstances in which the claimant is impecunious.⁶¹ But what does it mean for a claimant to be ‘impecunious’, so that access to justice considerations are engaged? Is it necessary that the claimant have no funds, or might it be the case that access to justice require that a claimant be able to engage the lawyer of their choice, out of liquid assets (for example)?

⁵⁹ *QPSX Limited v Ericsson Australia Pty Ltd (No 3)* [2005] FCA 933; (2005) 219 ALR 1, [54].

⁶⁰ *Unruh v Seeberger* (2007) 10 HKCFAR 31.

⁶¹ *Berman v SPF CDO I Ltd* [2011] 2 HKLRD 815 (CFI), [25]; *Chinachem Charitable Foundation Ltd v Chan Chun Chuen* [2011] HKEC 888 (CFI), [35]-[36].

In *Imam v Life (China) Company Limited*,⁶² the claimant had entered into a litigation funding agreement. He sought a declaration that the agreement was either not unlawful, or was protected by the access to justice exception, on the basis that he had insufficient funds to pursue the claim unaided.⁶³ The legal costs were estimated to be between approximately AU\$900,000 and AU\$1.2 million. The claimant's wife had liquid assets of approximately AU\$140,370 and illiquid assets of approximately AU\$1,224,380, about AU\$800,000 of which represented the value of the family home. The claimant was also a beneficiary of a family trust which held a property valued at AU\$2.85 million, and other assets valued at AU\$255,598.⁶⁴

The claimant had given evidence that he did 'not wish to be a litigant in person or to have to pursue my case in a financially constrained manner', and the funding agreement would enable him to instruct his choice of counsel, and would level the playing field with the defendants.⁶⁵

The court was unwilling to grant declaratory relief of the form sought in any event,⁶⁶ but nevertheless explained that⁶⁷

... the purpose of the access to justice exception is to ensure that a litigant can gain access to justice, not to facilitate access to his ideal or preferred legal representation.

⁶² *Imam v Life (China) Company Limited* [2018] HKCFI 1852.

⁶³ *ibid* [2]-[3].

⁶⁴ *ibid* [146]-[150].

⁶⁵ *ibid* [151].

⁶⁶ The court's reasoning on the questions whether the agreement fell foul of the prohibition of maintenance and champerty, and whether one of the exceptions applied, were therefore strictly obiter.

⁶⁷ *ibid* [152].

In the circumstances, the court did *not* consider that the claimant lacked the means to proceed with the litigation.⁶⁸ Further, the court considered it unlikely that a ‘financial imbalance’ between the parties would engage the access to justice exception.⁶⁹ Fee J did, however, see ‘some force’ in the argument that the claimant ought not to be expected to sell his family home to pay for the litigation.⁷⁰

The question of when the right of access to justice is engaged on financial grounds also arose before the English Supreme Court in the context of considering whether the imposition of certain fees was an impermissible fetter on the right of access to justice. It was there held that⁷¹

... The question whether fees effectively prevent access to justice must be decided according to the likely impact of the fees on behaviour in the real world. Fees must therefore be affordable not in a theoretical sense, but in the sense that they can reasonably be afforded. Where households on low to middle incomes can only afford fees by sacrificing the ordinary and reasonable expenditure required to maintain what would generally be regarded as an acceptable standard of living, the fees cannot be regarded as affordable.

The Court there referred to a series of sources of evidence that the fees had hindered access to the court: court statistics showing that the actual number of claims had fallen, particularly for low-value claims (where the level of fees was disproportionate to the likely award),⁷² court statistics showing that the level of fee remission had been lower than expected,⁷³ survey evidence indicating that large numbers of people had abstained from making claims because of the (in)affordability

⁶⁸ *ibid* [150].

⁶⁹ *ibid* [155].

⁷⁰ *ibid* [147].

⁷¹ *R (UNISON) (n 22)* [93].

⁷² *ibid* [38]-[42].

⁷³ *ibid* [43]-[44].

of fees,⁷⁴ and case studies of hypothetical claimants showing that people of apparently ordinary income and means would be ineligible for fee remission, and, if they paid the fees, would suffer a shortfall from the minimum income standards set by the Joseph Rowntree Foundation.⁷⁵

We can see, then, that the concept of providing access to justice for those who cannot afford litigation raises more questions than it answers. Are these concerns engaged if a litigant can afford litigation only by foregoing normal spending, or diverting resources from its business? What if a person can only afford an inexperienced lawyer? In England, how does it fit with the CPR objective of providing equality of arms?

Similar problems have been observed by commentators in the context of the Article 6 jurisprudence. The cases which address the right of ‘access to justice’ in the context of legal costs or fees involve extreme fact situations: a litigant in receipt of income support who is sued by McDonalds,⁷⁶ or who is required to pay a fee (substantially in excess of his weekly earnings) for issuing a writ irrespective of his means.⁷⁷ But, as McBride explains, there is little guidance on what facts are sufficient to engage access to justice on financial grounds:⁷⁸

... there is still uncertainty as to the point at which a person's financial resources make the provision of legal aid necessary. The cases have simply proceeded on the agreed basis that the applicants did not have the means to pay. Although there will be some individuals who have no

⁷⁴ *ibid* [45]-[49].

⁷⁵ *ibid* [50]-[55]. The Joseph Rowntree Foundation is a charitable foundation which (amongst other things) calculates and publishes minimum income levels which individuals and families would need to reach in order to provide for an acceptable standard of living (which includes items, such as social and cultural participation, which are arguably beyond the bare necessities of life).

⁷⁶ As in *Steel & Morris v United Kingdom* (2005) 41 EHRR 22; [2005] EMLR 15.

⁷⁷ As in *Ex parte Witham* (n 8).

⁷⁸ McBride (n 11) 259-60 [citations omitted].

resources, there is undoubtedly a line to be drawn between requiring a person to reduce themselves to absolute poverty and obliging them to draw upon resources not needed for simple existence in determining the amount that they can reasonably be required to contribute.

Conventional analysis asserts the access to justice benefits of litigation funding for the impecunious. But I suggest that this is an unprofitable way to think about litigation funding, not least because it is difficult to identify who is impecunious for this purpose. A more helpful way to think about litigation funding is to recognise that the high and unpredictable costs of litigation are a barrier to justice for all litigants (and may present an impenetrable hurdle for some).

The existing analysis does not explain or justify the litigation funding market as it presently exists

The doctrines of maintenance and champerty have been eroded, purportedly to provide access to justice for the impecunious and class action claimants. But the litigation funding market is frequently (and increasingly) serving claimants who could, if they diverted resources from their central business activities, afford litigation. It is therefore unsurprising that critics of litigation funding are sceptical about the ‘access to justice’ benefits of funding – if one adopts a conventional view about what ‘access to justice’ means, then it is fairly arguable that much of the litigation funding market does *not* promote access to justice.

In later chapters, I will consider the regulation of litigation funding. For present purposes, it is sufficient to observe that the discussion of whether and how the litigation funding industry ought to be regulated has, I suggest, been hindered (particularly in Australia) by a failure to start from first principles: to start by thinking about what the purpose of litigation funding is, and what are its effects.

One aspect of this is that the risks of litigation funding, and the possible market failures, have been poorly captured or articulated. For example, as was discussed in Chapter 3, some hostility to litigation funding is really a symptom of hostility towards litigation more generally. Conversely, as will be discussed in Chapter 9, little regulatory attention has been paid to the need to ensure the capital adequacy of the funder, which is a more pressing risk.

But another aspect is that the place of litigation funding in the civil justice system, and its potential benefits, have also not been properly captured or articulated. I suggest that this has impeded any debate about how funding might be regulated, and will return to this theme in later chapters.

Summary

Courts have considered that litigation funding promotes access to justice for the impecunious, and this has been a substantial factor in permitting the practice. This view is also seen in the commentary. But I suggest that it is an unhelpful way to think about the potential benefits of litigation funding. It does not account for the modern market, and does not accurately identify the barriers to litigation. It is, therefore, right that courts have been permissive in their attitudes to litigation funding, but courts and commentators have perhaps taken an overly simplistic view of its access to justice benefits.

I suggest, instead, that in considering the place of litigation funding in the modern civil justice system, two points are critical. First, funding is consistent with the values of the modern civil justice system. Secondly, it is a market response to a series of barriers to justice, which affect impecunious and well-resourced litigants alike.

Litigation funding and equality of arms

It is convenient here to deal briefly with another suggested benefit of litigation funding.

It is sometimes suggested that litigation funding creates an equality of arms between the parties, by equalising their financial resources.⁷⁹

It is desirable that a litigant has the same legal resources as the other litigant(s) with whom he is in dispute.⁸⁰ Indeed, the English CPR, in setting out the implications of the overriding objective, states that dealing with a case justly includes “ensuring that the parties are on an equal footing”.⁸¹ If litigation funding had a tendency to create an equality of arms, that would be a desirable consequence.

However, the argument that litigation funding is beneficial because it provides financial equality of arms has limited appeal. It is fair to assume that the defendant to funded proceedings will have means – a rational funder would only proceed if that were

⁷⁹ Rupert Jackson, *Review of Civil Litigation Costs: Preliminary Report* (2009), Chapter 15, [3.1]; The Law Reform Commission of Hong Kong, *Class Actions (Report)* (2012), [8.81(a)]; Andrew Watson and Michael Donnelly, ‘Financing Access to Justice: Third-Party Litigation Funding and Class Actions in Australia’ (2014) 55 *Canadian Business Law Journal* 17, 26-7; Charles M Wright and Anthony O’Brien, ‘Third-Party Funding for Class Actions, and Control over the Litigation’ (2014) 55 *Canadian Business Law Journal* 165, 165-7.

The point is not uncontroversial; a diversity of suggestions are made as to likely effects of litigation funding on overall costs, and on settlement incentives: see, eg, Stephen Gillers, ‘Waiting for Good Dough: Litigation Funding Comes to Law’ (2010) 43 *Akron Law Review* 677, 691-5; Alexander Bruns, ‘Third-Party Financing in the Perspective of German Law - Useful Instrument for Improvement of the Civil Justice System or Speculative Immoral Instrument?’ (2012) 8 *Journal of Law, Economics and Policy* 525, 537-9; Nora Freeman Engstrom, ‘Re-Re-Financing Civil Litigation: How Lawyer Lending Might Remake the American Litigation Landscape, Again’ (2013) 61 *UCLA Law Review Discourse* 110, 119, 121; Poonam Puri, ‘Profitable Justice: Aligning Third-Party Financing of Litigation with the Normative Functions of the Canadian Judicial System’ (2014) 55 *Canadian Business Law Journal* 34, 45-6; Charles Silver, ‘Litigation Funding versus Liability Insurance: What’s the Difference?’ (2014) 63 *DePaul Law Review* 617, 641-4; Jef De Mot and Michael G Faure, ‘Third-Party Financing and Litigation Expenditures’ (2016) 12 *New York University Journal of Law and Business* 751.

⁸⁰ Frederick Wilmot-Smith, *Equal Justice: Fair Legal Systems in an Unfair World* (Harvard University Press 2019), 71, 74-6.

⁸¹ CPR 1.1(2)(a).

the case.⁸² However, it is a mistake to treat the cohort of defendants to funded proceedings as homogenous. Some defendants may be asset-rich and cash poor. Even if they are well-resourced, defendants who are government authorities or charities may well have to divert funds from worthy causes in order to satisfy an adverse judgment or costs order, and of course corporate defendants might have to divert money from their business activities. Thus, even a well-resourced defendant might have a limited appetite for litigation. Further, as explained in Chapter 6, claimants using funding are diverse. Many are well-resourced and could, in fact, fund their own litigation.

Whether there is equality of arms between the parties is contingent on the unique circumstances of the claimant and defendant. In some cases, litigation funding might lead to an equality of arms between the parties (in the sense of equalising their financial resources available for litigation) but this is contingent, and the parties' appetite for litigation might depend on broader considerations than availability of funds.

It seems more plausible that the use of litigation funding might promote equality of arms between powerful and vulnerable litigants in a more subtle way. Galanter described two categories of litigant – the “Repeat Players” and the “One-Shotters”.⁸³ Repeat players have a variety of advantages in litigation.⁸⁴ These include better access to lawyers, and the ability to take a long-term view of litigation – for example, by choosing which cases to settle and which to pursue in order to drive rule-change. Their repeat status means that they have a reputation before the court.

⁸² As discussed in Chapter 6.

⁸³ Marc Galanter, ‘Why the “Haves” Come out Ahead: Speculations on the Limits of Legal Change’ (1974) 9 *Law and Society* 95, 97.

⁸⁴ *ibid* 98-103.

One-shot players lack these advantages. The involvement of lawyers on their behalf (who are, themselves, repeat players) does not mitigate the problem.⁸⁵ Lawyers are unable, for example, to devise long-term litigation strategies by treating each individual client as analogous to a single claim for a repeat player.

Galanter identifies that one way of rectifying the problem is for one-shotters to form informal alliances, such as through trade unions or interest groups.⁸⁶ But the presence of a litigation funder might also serve to confer benefits of a repeat player on a one-shotter. Steinitz, for example, suggests that funders might be able to coordinate individual claimants so that they might, to a limited extent “play for rules” – that is, litigate strategically so that the development of the law favours the class to which the claimant belongs.⁸⁷ Molot suggests that funders can, effectively, increase the risk appetite of claimants, meaning that they are not disadvantaged at the point of settlement as a one-shotter might otherwise be.⁸⁸ Further, given the incentive of a funder to back only meritorious cases, the involvement of a funder arguably provides a “signal” of the value of the claim,⁸⁹ which might again strengthen the claimant’s hand at the point of settlement negotiations.

The possibility that funders might litigate strategically, with a view to effecting legal change, is most prevalent in the US literature. There is a history of strategic

⁸⁵ *ibid* 114-117.

⁸⁶ *ibid* 141.

⁸⁷ Maya Steinitz, ‘Whose Claim is this Anyway? Third-Party Litigation Funding’ (2011) 95 *Minnesota Law Review* 1268, 1299-1310.

⁸⁸ Jonathan T Molot, ‘Litigation Finance: A Market Solution to a Procedural Problem’ (2010) 99 *The Georgetown Law Journal* 65, 89.

⁸⁹ Ronen Avraham and Abraham Wickelgren, ‘Third-Party Litigation Funding - A Signaling Model’ (2014) 63 *DePaul Law Review* 233, 235 argue that the presence of funding might in fact be a signal to the *court* regarding the merits of the claim.

litigation to effect legal change in the US,⁹⁰ the success of which has ultimately led to attempts to restrict such litigation by those who oppose the substance of the changes effected, or who oppose judicial legislation.⁹¹ Thus, as a counterpoint to the argument that funders might aid “one-shotters”, it is suggested that a critical risk of funding is the potential for funders to engage in ‘path manipulation’, by selecting cases (and the sequence in which they will be litigated) in order to drive precedent in a particular direction.⁹²

There is some empirical support for the suggestion that funders have been able to drive developments in the law. As will be explained in Chapter 9, funders have, in the Australian class action context, driven the development of the law governing litigation funding.⁹³ In simplified terms, funders have sought – and obtained – court approval for various aspects of their business practices. A body of case law concerning the use of litigation funding in class actions has thus developed, incrementally. The changes to the law have benefitted funders, and the court has been motivated to facilitate litigation funding, because in the absence of external funding the class action regime would have been unworkable.⁹⁴

But it is suggested that this is a relatively limited, and more subtle effect than many commentators assert. Any long-term litigation strategy by a repeat player may

⁹⁰ The most obvious example is the NAACP’s strategic litigation campaign culminating in *Brown v Board of Education of Topeka* 347 US 483 (1954).

⁹¹ Mark Tushnet, ‘Some Legacies of *Brown v Board of Education*’ (2004) 90 *Virginia Law Review* 1693, 1695-1705.

⁹² Paul H Rubin, ‘Third-Party Financing of Litigation’ (2011) 38 *Northern Kentucky Law Review* 673, 682-5; Jeremy Kidd, ‘To Fund or not to Fund: The Need for Second-Best Solutions to the Litigation Finance Dilemma’ (2012) 8 *Journal of Law, Economics and Policy* 613, 629-31.

⁹³ Michael Legg, ‘Current Trends in Australian Shareholder Class Actions’ (Presentation to Australian Insurance Law Association, Sydney, 19 August 2015), 18.

⁹⁴ See, eg, Michael Legg, ‘Reconciling Litigation Funding and the Opt Out Group Definition in Federal Court of Australia Class Actions - the Need for a Legislative Common Fund Approach’ (2011) 30 *Civil Justice Quarterly* 52, 58 (closed classes).

accelerate the process of precedent development. But it does not follow that this will drive changes in the law which ought not to have happened.

Conclusion

In this chapter, I have explained that litigation funding promotes access to justice beyond its use by impecunious and class action claimants (which are the categories usually referred to by judge and commentators). Rather, litigation funding promotes access to justice by removing or mitigating a variety of barriers to justice:

- the high cost of litigation (that is, the high cost of litigation in absolute terms);
- the high cost of litigation relative to the amount claimed;
- the unpredictability of litigation costs;
- the difficulty and complexity of litigation; and
- the inherent conflict of interest which exists between lawyer and client when a lawyer is retained on an hourly rate basis.

These barriers may be experienced even by well-resourced and powerful claimants.

Conventional analysis focuses on the access to justice benefits for the impecunious. But, as I have explained here, this may be an unhelpful and overly limited way to think about the role of litigation funding in the civil justice system. In any event, it is difficult to define precisely who the ‘impecunious’ are for this purpose.

Thinking about the ‘access to justice’ benefits of litigation funding in broader terms has two benefits. First, it enables us to better assess the role or place of litigation

funding in the civil justice system. Secondly, it will enable a fuller discussion of the regulatory options for the industry.

CHAPTER 8: WHAT ARE RISKS OF LITIGATION FUNDING, AND SHOULD THEY BE REGULATED?

Introduction

The first part of this thesis has addressed the principled objections to litigation funding, including those expressed through the doctrines of maintenance and champerty. I have proposed that litigation funding, as a matter of principle, ought to be accepted as an uncontroversial, if not beneficial, feature of the civil justice landscape.

The remainder of this thesis turns to more practical matters: identifying the potential risks of litigation funding, and whether (and if so, how) they ought to be regulated.

This chapter identifies the sorts of market failures which might exist in the litigation funding market, and also some general theory regarding regulation. The next chapter sets out the current state of regulation (which is piecemeal, and unsatisfactory). The final two chapters then address the particular difficulties which might emerge in the litigation funding industry, and makes some modest proposals for regulation.

Understanding market failures

Regulation is most commonly assessed against economic goals.¹ A market may be judged in economic terms by the efficiency of the outcomes it produces. An efficient

¹ Anthony I Ogus, *Regulation: Legal Form and Economic Theory* (Hart Publishing 1994), 1, 4. See also Mike Feintuck, 'Regulatory Rationales Beyond the Economic: In Search of the Public Interest' in Robert Baldwin, Martin Cave and Martin Lodge (eds), *The Oxford Handbook of Regulation* (Oxford University Press 2010), 39-42.

outcome occurs where resources are distributed to their most valuable use.² Economic analysis starts from the position that resources will be allocated in an efficient manner if the market is perfectly competitive.³

Market failures are features of a market which inhibit competition. They are undesirable because they lead to inefficient allocation of resources, which is wasteful.

There are many types of market failure.⁴ The most relevant varieties of market failure for the purpose of considering the litigation funding market are:

- *Negative externalities* – these occur where a transaction between buyer and seller fails to capture the true cost of the good or service, because at least part of the cost is imposed on a third party. A classic example is the purchase of goods which are produced in circumstances which harm the environment. The price of the good will not reflect the true cost, because the buyer and seller do not suffer the full effect of the harm.⁵ But negative externalities might equally affect one, identifiable third party.⁶
- *Incomplete information; information asymmetries* – a different market failure occurs where one party to a transaction has insufficient information to make an informed choice, or one party has more

² Ogus (n 1) 22; Cento Veljanovski, 'Economic Approaches to Regulation' in Robert Baldwin, Martin Cave and Martin Lodge (eds), *The Oxford Handbook of Regulation* (Oxford University Press 2010), 20.

³ Ogus (n 1) 22; Veljanovski (n 2) 19-20.

⁴ See, eg Cass Sunstein, *After the Rights Revolution: Reconceiving the Regulatory State* (Harvard University Press 1990), 48-55; Robert Baldwin, Martin Cave and Martin Lodge, *Understanding Regulation: Theory, Strategy, and Practice*, vol 2 (Oxford University Press 2012), 15-22; but cf Veljanovski (n 2) 20-2.

⁵ Ogus (n 1) 35-8; Veljanovski (n 2) 21; Baldwin (n 4) 18.

⁶ Sunstein (n 4) 54.

information than the other. They may arise for a variety of reasons. For example, the seller may have insufficient incentive to provide the information, or there may be some benefit to them in concealing information from the buyer. This is harmful to competition, as it means that even a rational buyer may fail to select the most valuable alternative – a problem known as adverse selection.⁷

- *Moral hazard* – broadly speaking, a moral hazard arises where a person has no incentive to avoid the risk of negative outcomes, because any such negative outcomes will be borne by a third party. The beneficiary may, therefore, have an incentive to alter their behaviour (and take more risk), particularly if they will benefit from any positive outcome of taking the risk in question. A classic example from the financial crisis is that if a bank knows that it will be bailed out by the government in the event of a crisis, it has little incentive to avoid risk-taking, particularly if it stands to make large profits if the risk-taking pays off. An equivalent problem occurs when a third party assumes a responsibility to pay for goods or services on behalf of a beneficiary. The risk to competition is that the consumer will use more of the good or service than is optimum.⁸ So, for example, where healthcare is paid for entirely by the government, there is a risk that patients will over-use services.

⁷ Sunstein (n 4) 52-3; Ogus (n 1) 35-41, and see generally Chapter 7; Veljanovski (n 2) 22; Baldwin (n 4) 18-19.

⁸ Baldwin (n 4) 20. But cf Veljanovski (n 2), who treats this as an aspect of information asymmetry.

- *Inequality of bargaining power* – inequality may be caused by information asymmetry. It might also be caused by the position of the counterparties: for example, a person who is forced to sell a good or service out of necessity is unlikely to secure the optimum price.⁹ It threatens competition because it means price is affected by a factor which is contingent (i.e. relative bargaining power), and irrelevant from the perspective of the market.

As will be seen, there is a risk of each of these market failures occurring in the litigation funding market, and evidence that some in fact occur.

The use of regulation to correct market failures is common. The form of regulation will depend on the type of market failure. For example, information asymmetries might be solved by mandating the provision of information by the seller to the buyer, or by regulators taking direct steps to provide relevant information to buyers. On the other hand, inequality of bargaining power might be ameliorated by facilitating collective bargaining (as in the labour market); another technique might be to outlaw certain types of sales altogether, if their character is such that they are inherently likely to involve an element of coercion.¹⁰

⁹ Baldwin (n 4) 20.

¹⁰ Michael J Sandel, 'What Money Can't Buy: The Moral Limits of Markets' (The Tanner Lectures on Human Values, Oxford, 11 and 12 May 1990), 94-5; Michael Sandel, *What Money Can't Buy: The Moral Limits of Markets* (Allen Lane 2012), 109-13.

Market failures in the litigation funding market

Information asymmetry

An important market failure in the litigation funding market (based on the data which presently exists) is the information asymmetry which exists between funder and claimant. There are two areas in which a claimant might lack relevant information. First, it may be difficult for the claimant to assess the risk that a funder will run out of funds during the course of litigation – the ‘capital adequacy’ risk. Whilst a funder’s financial information might be available (such as cash at bank), a claimant cannot fully assess the capital adequacy risk, because they do not know the extent of the funder’s other funding commitments. Further, it has been suggested that claimants do not adequately understand the importance of capital adequacy, meaning they would be unlikely to seek out this information.

Secondly, it may be difficult for a claimant to compare funders against each other, in order to obtain the best terms. There are three reasons for this information asymmetry. First, for many claimants – even sophisticated commercial claimants – litigation may be a rare occurrence. Seeking litigation funding is even rarer. A claimant may therefore lack the expertise necessary to evaluate the terms of a funding agreement, including even fundamental matters such as the funder’s percentage return. Secondly, the process of due diligence might restrict a claimant’s ability to compare funders on a like-with-like basis. The process can be time-consuming, and most funders require exclusivity during this period. This makes comparison between potential funders difficult, if not impossible. Thirdly, in the class action context, it is not uncommon for the funder to offer funding on standard terms, on a ‘take it or leave it’ basis (sometimes via a website). A claimant presented with a funding offer in this form may be unable

to negotiate terms, and the lack of negotiation may lead to terms being offered on a basis which is unclear.

There is already a partial market solution to this problem. Funding brokers claim to be able to assist claimants by identifying funding options available, and obtaining a selection of offers.¹¹ However, the use of a broker increases the cost of funding. This is because brokers typically charge an additional commission on top of the funding percentage.

The difficulty in comparing litigation funders means that there is an information asymmetry between the funder and the claimant. It has a tendency to diminish competition between funders.

A further information asymmetry: the strength of the claim

Until this point, I have identified information that the claimant does not have, or information asymmetries that operate to the advantage of the funder. However, there is an information asymmetry which operates in the other direction. A claimant has access to more information about their claim than the funder. A claimant may have access to, or knowledge of, any or all of the following:

- details about the events which gave rise to the cause of action, and possible defences;
- communications with the defendant, which might indicate the defendant's likely defence to any claim, or may include concessions by one or other party; and/or

¹¹ TheJudge, 'TheJudge is Pleased to Announce Our QI Litigation Funding Service' (2012) <<https://www.thejudgeglobal.com/thejudge-is-pleased-to-announce-our-qi-litigation-funding-service/>> accessed 3 August 2020; TheJudge, 'Case Example: How Much do Litigation Funders Prices Differ for Large Cases?' (2014) <<https://www.thejudgeglobal.com/case-example-how-much-do-litigation-funders-prices-differ-for-large-cases/>> accessed 3 August 2020.

- legal advice about the prospects of success of the claim (including advice from lawyers who are no longer retained).

This information affects the value of the claim. The funder can only obtain this information from the claimant.

Furthermore, the claimant may not be an entirely reliable source of information. For example, the claimant may not be entirely candid about the facts and circumstances giving rise to the claim. A claimant may fail to appreciate the significance of some piece of information. A corporate claimant, or an insolvency practitioner, may not have collated sufficient information from the employees or officers of the company.

Four consequences flow from this information asymmetry. First, it necessitates due diligence, which is an additional expense of litigation funding. The cost of due diligence – including for claims which will not ultimately be funded – is an overhead that the funder must recover from its profit on funded claims. Secondly, it has a tendency to increase the cost of funding, because the funder must take account of the risk that it is not fully informed about the claim. Thirdly, it increases the risk that unmeritorious claims may be commenced, because the claimant, who is best-placed to assess merits, has no incentive not to commence (because they are funded on a non-recourse basis), and the funder may not be able to assess properly the merits of the claim (in other words, there is a moral hazard). Fourthly, if a funder discovers facts during the course of litigation which alter its view of the merits of the claim, a funder's right to terminate the funding agreement might be triggered. It may be necessary to discontinue, either because the merits do not justify continuing, or because the claimant cannot continue in the absence of funding.

This information asymmetry is detrimental to both funder and claimant. It increases the risk for the funder, and increases the cost of funding to the claimant. Insofar as it increases the risk of unmeritorious claims being brought, or the risk of a funder later terminating the funding agreement, there is also an externality, in the form of detriment to the defendant and the court system.

This information asymmetry cannot easily be corrected by regulating the relationship between funder and claimant. Mandating the provision of information is likely to be otiose: funders already require the provision of information during due diligence. Further, some of the possible reasons for failure to disclose which were suggested above – such as failing to appreciate the significance of a piece of information – would not be corrected by an obligation of disclosure.

Disparities in bargaining power

The extent of any disparity in bargaining power between the funder and the claimant will obviously be contingent on the circumstances of the claimant. Two factors may affect a claimant's bargaining power: first, whether they are driven to use litigation funding by necessity, and, secondly, whether they are likely to be repeat users of funding.¹² At one end of the spectrum is the impecunious claimant who is a one-time litigant. Their use of litigation funding may well be driven by necessity, they may well be inexperienced litigators, and they cannot use the promise of further business to drive a funder towards more advantageous terms. In the class action context, terms may be offered by funders with no possibility of negotiation.

¹² See generally Nigar Hashimzade, Gareth Myles and John Black, *A Dictionary of Economics* (5th edn, Oxford University Press 2017), 'bargaining power' as to some of the general factors which might affect bargaining power.

At the other end of the spectrum is the large corporate who uses litigation funding as a risk management tool, or to improve their balance sheet, either on a single-claim basis or on a portfolio basis. They are not driven by necessity, may have experience of litigation, and may have established relationships with law firms (and perhaps in house counsel). Further, the likelihood of repeat business may encourage funders to offer better terms.

Negative externalities

The existence of a funding agreement between funder and claimant has the potential to affect two other groups of people: the defendant, and the court system. For example, if the funder runs out of capital and is unable to continue funding, then the defendant is affected insofar as it will not be paid adverse costs, and the court system is also affected.

Thus, if an impecunious claimant fails to negotiate for the funder to pay adverse costs, and/or fails to ensure that the funder is well-capitalised, there is a risk to the defendant, and to the court – in fact, the claimant might suffer no adverse consequences. The defendant and the court cannot protect themselves from this risk.

Moral hazard

The moral hazard which operates is the risk that a claimant will conduct the litigation in a way which causes more legal costs than is optimal – for example, by instructing the lawyers to undertake a disproportionate amount of work, or by refusing to accept a settlement offer and therefore prolonging litigation. Unlike most of the risks identified above, this risk has the potential to affect adversely the funder.

There are, however, a variety of ways in which the litigation funding market has dealt with this problem – either by contract, or the funder exerting some degree of

control, or due diligence. So, for example, in response to the risk that the claimant will use more legal resources than is optimal:

- the funder will take into account who is the lawyer, and may even nominate the lawyer, or veto the claimant's choice;
- the funder will take into account the motivation of the claimant in deciding whether to fund the claim;
- the funding contract might be drafted to align the interests of the funder and the claimant;
- in Australia particularly, the funder will exert some measure of control, and may provide instructions to the lawyer
- funding agreements deal with disputes over settlement, and the industry self-regulation codes in England and Australia¹³ identify a dispute resolution process;
- there are caps on spending, and/or the lawyers work on conditional fee agreements; and
- the funder may review and approve bills, and challenge line items.

Summary

Standing back, we can see that there are two market failures which are likely to affect *funders* – the information asymmetry *insofar as it relates to the strength of the claim*, and the moral hazard that the claimant will use more legal resources than is optimal. Each of these is largely dealt with by the market already, either through the funder

¹³ These will be discussed further in the following chapter.

requiring a due diligence period, and/or by incorporating terms into the funding agreement which address the problem.

On the other hand, there are a range of market failures which are more likely to adversely affect the claimant, or third parties. These are not well-regulated, either by market practice, or by regulation.

In summary, there are six potential areas of difficulty:

- percentage return;
- control;
- capital adequacy;
- termination;
- adverse costs; and
- disputes between funder and claimant.

The first three might arise because of disparities in bargaining power; the last three involve externalities.

Tailored regulation?

One difficulty in regulating the litigation funding industry is that overly prescriptive regulation might prevent valuable agreements. For example, one of the risks of litigation funding which will be addressed in detail in the next chapter is the risk that the funder might seek too great a percentage of the recovery. But imposing a cap on the funding percentage return might stifle litigation which is socially valuable but risky (for example, because it involves an unsettled point of law), and will likely be too broad-brush.

Regulation ought to be as light-handed as possible. Any regulation imposes on parties' freedom of contract. It ought to do so only as far as is necessary to address the market failures to which it is targeted, or to promote some social value, such as protecting vulnerable claimants. Further, regulation may be expensive.

Another difficulty is that the claimants who seek funding are diverse. As explained in Chapter 6, some claimants will be inexperienced 'one-shotters', and others will be experienced repeat players. An obvious example of the latter group are insolvency practitioners. An insolvency practitioner might be very experienced in litigation, and is also a potential repeat client of a funder, and so has bargaining power. They might therefore be well-placed to bargain for terms which are appropriate to their preferences and circumstances.

A risk of regulation is therefore that it will unnecessarily inhibit funding agreements, and impose unsuitable 'one-size-fits-all' solutions on parties who are sufficiently powerful, experienced and/or sophisticated to bargain for better solutions.

On the other hand, for smaller claims, it might be inefficient and disproportionately costly to encourage claimants to negotiate all terms of a funding agreement, even if they are appropriately informed and advised about all relevant risks. So, although taking independent advice from a lawyer might enable a claimant to achieve the optimum funding agreement for their particular circumstances, the cost of this may be disproportionate to the size of the claim. It may be more cost-effective, and lead to better outcomes, if standard terms were to apply, particularly in respect of matters such as dispute resolution procedures, where there could be economies of scale if the procedures were to be administered on an industry-wide basis.

One might question, therefore, whether all market participants ought to be subject to the same regulation.

One way to tailor regulation would be to impose different regulatory requirements on different sectors of the litigation funding market – for example, distinguishing between class actions, insolvency actions, and other litigation. This has some appeal, because the risks and difficulties in each context are slightly different. Or, it might be possible to tailor regulation based on the characteristics of the claimant, such as their means, sophistication and experience. The concept of tailored regulation is considered in the remainder of this chapter.

Tailoring consumer protection regulation so as to exclude sophisticated consumers

There are numerous regulatory laws in England and Australia which have the purpose of protecting consumers in particular transactions, but which exclude certain categories of consumer (sometimes referred to as ‘sophisticated consumers’, or similar) from their scope.¹⁴ There is good reason for doing this. As discussed earlier, regulation imposes

¹⁴ In what follows, I refer to legislation which is either of general application to all contracts, or is applicable to contracts which are in some way analogous to litigation funding agreements. This includes:

Legislation regulating Australian conditional costs agreements: Legal Practitioners Act 1981 (SA); Legal Profession Act 2006 (ACT); Legal Profession Act 2006 (NT); Legal Profession Act 2007 (Qld); Legal Profession Act 2007 (Tas); Legal Profession Act 2008 (WA); Legal Profession Uniform Law (NSW); Legal Profession Uniform Law (Vic).

Legislation regulating consumer contracts: Australian Securities and Investment Commission Act 2001 (Cth), Division 2, Part 2; Competition and Consumer Act 2010 (Cth); Consumer Rights Act 2015 (UK); Consumer Protection from Unfair Trading Regulations 2008/1277.

Legislation regulating consumer credit transactions: Consumer Credit Act 1974 (UK); the National Credit Code, which is Schedule 1 to the National Consumer Credit Protection Act 2009 (Cth).

Financial services legislation: Corporations Act 2001 (Cth); see Department of Treasury, *Wholesale and Retail Clients: Future of Financial Advice* (2011), 2.1 and 2.7; see also Australian Securities and Investment Commission, *Senate Inquiry into Consumer Protection in the Banking, Insurance and Financial Sector: Submission by the Australian Securities and Investments Commission* (2017), [134] as to the introduction of distinctions between different

additional cost and administrative burdens. Unnecessary regulation is, therefore, inefficient. Excluding sophisticated consumers from the operation of consumer protection laws therefore serves to ensure that vulnerable consumers are protected, but that no additional regulatory burden is imposed in respect of consumers who do not need protection.

The regulatory laws which distinguish between different types of consumers are diverse. At one end of the spectrum, the Australian Consumer Law and the English Consumer Rights Act 2015 provide various consumer protections to individuals when they engage in day-to-day transactions. This is a broad-brush distinction: a class of transactions is captured by reference to the simple test of the purpose of the transaction.

At the other end of the spectrum, there are various statutes in England and Australia regulating financial services which distinguish between consumers for the purpose of, for example, equity raising. For example, securities cannot be offered to the public without a prospectus – unless the offer is made only to sophisticated and/or professional investors. These investors might be defined by their income or assets, or whether they are licensed to transact in particular markets. In this realm, it has been said that distinguishing between different classes of consumer is intended to serve the dual purpose of protecting consumers, whilst also enabling wholesale and sophisticated individual clients to access wholesale markets (which often trade more complex products) and avoid the ‘hindrance’ of the increased regulatory burden.¹⁵ More specifically, it has been ‘recognised’ that ‘wholesale clients do not require the same

forms of consumers in that legislation; Financial Services and Markets Act 2000 (UK); Financial Services and Markets Act 2000 (Financial Promotion) Order 2005/1529; *Bailey v Barclays Bank Plc* [2014] EWHC 2882 (QB); *Conduct of Business Sourcebook* (2018); FCA Handbook - Glossary (Release 32, Oct 2018).

¹⁵ Department of Treasury (n 14) 2.1 and 2.7.

level of protection, as they are better informed and better able to assess the risks involved in financial transactions'.¹⁶ There is, accordingly, no need to inhibit their freedom of contract.

The grounds on which consumers are distinguished for the purpose of consumer protection laws include the following:

- simple distinctions on the basis of the status of the individual (more usual for common, day-to-day transactions, which may be small in quantum):
 - whether the consumer is an individual or a business;
 - whether the transaction is for a personal/domestic or business purpose;
- more complex distinctions which seek to distinguish between progressively more sophisticated consumers (more usual where the transaction in question is relatively unusual and infrequent, and is likely to involve a large quantum), which include:
 - the qualifications and/or experience of the consumer, where they are an individual;
 - the income and/or asset base of the consumer, or (in the case of businesses) the number of employees;
 - the size of the transaction in question;
 - whether the consumer has relevant professional credentials.

For individuals, this might include whether they are, in effect, a professional investor. For businesses, this might include

¹⁶ The Parliament of the Commonwealth of Australia, *Financial Services Reform Bill 2001 - Explanatory Memorandum* (2001), [2.25].

whether they have financial services licence (for example), which would again indicate whether the business regularly engages in transactions of the sort in question.

There are numerous regulatory provisions in which consumers are able, in effect, to decide whether or not to exempt themselves from consumer protection provisions. These provisions may take the form of:

- enabling the consumer to make a declaration as to the purpose of the transaction and/or whether they meet the criteria for ‘opting out’ of the consumer protection regime;
- requiring the counterparty to make an assessment of the consumer’s status; and/or
- requiring the consumer to provide evidence from a third party (such as an accountant) as to their status.

Finally, the form of consumer protection takes a variety of forms:

- requirements that the counterparty provide the consumer with certain information;
- voiding certain terms of contracts – for example, terms which are ‘unfair’ within the meaning of the Australian Consumer Law, or the Consumer Rights Act 2015;
- limits on fees and/or interest rates (in the context of consumer credit agreements) – i.e. setting boundaries on the permissible terms;
- disempowering consumers from entering into particular types of transactions, unless they can be categorised as ‘sophisticated’ consumers; and

- providing additional causes of action and/or procedural means for pursuing complaints, which might only be available to a subset of consumers regarded as vulnerable.

As will be explained in the next section, a critical issue in tailoring regulation to the sophistication of the consumer is identifying where to draw the line.

Problems with tailored regulation

Tailored regulation is not without risks. A first risk is that if regulation applies to only a subset of claimants, funders may well be less willing to enter into agreements with that subset.

A second problem is the adverse consequences of failing to draw the line between sophisticated and unsophisticated consumers in an appropriate place. The problem is well-illustrated by the facts described in *Wingecarribee Shire Council v Lehman Brothers Australia Ltd (in liq)*.¹⁷ The three ‘sample’ claimants in a class action were local government authorities, each of which had a conservative investment policy and substantial funds for investment.¹⁸ However, none of the employees who had responsibility for managing these funds had any experience or qualifications in sophisticated investment products – which was why they sought advice from Lehman. Lehman recommended investments which did not meet the councils’ investment criteria, and was therefore held to have acted in breach of its contractual agreements, as well as being negligent, and in breach of the ASIC Act obligations concerning misleading and deceptive conduct.

¹⁷ *Wingecarribee Shire Council v Lehman Brothers Australia Ltd (in liq)* [2012] FCA 1028; (2012) 301 ALR 1.

¹⁸ About \$15 million in the case of Swan ([156]), about \$28 million in the case of Parkes ([505]) and about \$50 million in the case of Wingecarribee ([617]).

The case illustrates two points. First, the councils were aware of the limitations of their own knowledge and expertise – and, indeed, sought external advice for that reason. Nevertheless, they were outside the consumer protections offered to retail clients, because they fulfilled certain criteria. Secondly, it provides an example of a situation in which meeting certain criteria was *not* indicative of the financial sophistication of the customer in question.

In 2011, the Australian Department of Treasury considered the appropriateness of the distinction between retail and wholesale investors in the Corporations Act.¹⁹ The question arose because of the concern that prior to the GFC, investments had been made (and substantial sums lost by) wholesale clients who had fallen outside consumer protection laws.²⁰ The resulting options paper identified the potential for anomalous application of the definitions. For example, a small business was treated as a retail client, and precluded from certain investments, but a person meeting the income threshold was treated as sophisticated, despite evidence suggesting an imperfect relationship between income and financial literacy.²¹

Similarly, the prohibitions against unconscionable conduct in the Australian Consumer Law and the ASIC Act are *not* applicable where the counterparty is a publicly listed company.²² But a recent report by Consumer Affairs Australia and New Zealand has questioned this carve-out, arguing that public listing is not necessarily indicative of a party's size, resources or 'ability to withstand unconscionable conduct', and that it created anomalous results because publicly listed companies might be

¹⁹ Department of Treasury (n 14).

²⁰ *ibid* 1.2, and Section 4.

²¹ *ibid* Section 5.

²² Australian Securities and Investment Commission Act 2001 (Cth), s 12CB; Competition and Consumer Act 2010 (Cth), Schedule 2, s 21(1).

smaller than private companies which would have the benefit of the protection.²³ It therefore recommended that the unconscionable conduct protections in the ACL and the ASIC Act apply to all counterparties, including publicly listed companies.²⁴

The Australian experience is by no means unique. In England, in the wake of the GFC, concern about the mis-selling of complex investment products to local authorities led to their being recategorised as retail clients, and thus subject to various consumer protection rules (authorities were able to elect to be treated as professional clients if they satisfied certain criteria).²⁵ The difficulty in crafting an appropriate test for ‘sophistication’ was also demonstrated when, in 2013, the Financial Services Authority (‘FSA’) established a review into the sale of interest rate hedging products (‘IRHP’) to ‘non-sophisticated’ customers. It adopted, as the criteria for ‘sophistication’, whether the company would be treated as small enterprises for the purposes of the Companies Act 2006. However, in its pilot findings, the FSA reported that it had been necessary to amend the criteria because enterprises such as farms and bed and breakfasts – which met the asset threshold because of property holdings, and met the employee thresholds because of seasonal workers – were excluded from the IRHP review. The FSA regarded this as an anomalous and unintended result.²⁶

The difficulty in each case seems to have been that unsophisticated customers were automatically excluded from consumer protection regimes, because they met

²³ Consumer Affairs Australia and New Zealand, *Australian Consumer Law Review - Final Report* (2017), 48.

²⁴ *ibid* 50.

²⁵ Financial Conduct Authority, *Markets in Financial Instruments Directive II Implementation – Consultation Paper III (CP16/29)* (2016), Section 4; Financial Conduct Authority, *Markets in Financial Instruments Directive II Implementation – Policy Statement II (PS17/14)* (2017), Section 8; Financial Conduct Authority, *Conduct of Business Sourcebook* (2018), [3.5.2B]-[3.5.9].

²⁶ Financial Services Authority, *Interest Rate Hedging Products - Pilot Findings* (2013), 10-12.

certain threshold criteria. Introducing further nuance into threshold criteria is unlikely to be a complete solution; it is impossible to regulate at a granular level, nor to anticipate all likely effects. A better solution is likely to be to require consumers to opt out of protection.

Which claimants ought to be included in and excluded from a regulatory scheme?

Following the description of the litigation funding market in Chapter 6, we can divide funded claimants into the following categories:

- Insolvency practitioners.
- Class action claimants – this is a potentially very wide category, ranging from individuals who may have limited means, no experience of litigation and little engagement with the litigation process, through to large corporate entities (such as institutional investors). It may include claimants who are using litigation funding through necessity, and those who are using it as a ‘risk management’ tool, or in order to secure the benefit of proceeding as a class (such as the economies of scale).
- Claimants who could afford to pay for their own litigation, but use litigation funding as a ‘risk management’ device, and thereby avoid the unpredictability of costs (including adverse costs) in exchange for giving up part of their recovery.
- Claimants who use litigation funding through necessity. This is a potentially diverse group. At present, most litigation funding in Australia and England is for relatively high-value claims, which might be expected to have high costs – although there are signs that the market is expanding

to include lower-value claims too. The litigants who use funding out of necessity may, therefore, range from inexperienced individuals who could not afford any expenditure on legal fees, through to commercial enterprises which might be sophisticated and substantial, but nevertheless unable to afford legal fees owing to the size of the claim and its anticipated cost, or the competing demands on their resources.

The border between the third and fourth categories might be extremely difficult to determine. This is well-illustrated by the Hong Kong jurisprudence concerning the extent of the ‘access to justice’ exception to the rule against maintenance and champerty, discussed in Chapter 7, which has required the court to assess at an extremely granular level the resources of a claimant, and to make judgments about the level of legal expenditure which is reasonable for a party.

Insolvency practitioners are an obvious candidate group for exclusion from regulation. They are experienced and professional litigators, and as such can be expected to have some knowledge of the litigation process, an ability to negotiate with funders, and to be sophisticated consumers of legal services. They can also be expected to have a degree of bargaining power as ‘repeat players’ in the market. Further, it is simple to demarcate the group excluded from a regulatory regime – the criterion is simply whether the litigation is brought by an insolvency practitioner for the benefit of a company which is subject to an insolvency process.

At the other end, class action claimants are a diverse class. However, there is good reason to treat them as a unified class for regulation purposes. As identified above, one of the risks of regulation is that it imposes additional costs and administrative burdens. If regulation is limited to unsophisticated consumers, then it is rational for funders to prefer to enter funding agreements with sophisticated consumers.

This creates a potential difficulty given the acceptance (in Australia, at least) of closed classes. A funder could potentially enter into funding agreements only with sophisticated consumers, and then commence a class action which was limited to those consumers. This would have obvious access to justice consequences, and would be contrary to the very purpose of the class action procedure. In England, and in open classes in Australia, it might be practically difficult to apply different regulatory requirements between different groups of claimants.

Accordingly, class action claimants ought to be included in a regulatory regime, irrespective of the sophistication of the individual litigant.

The task then is to identify which other litigants ought to be excluded from any regulatory scheme. An important difficulty is in drawing the line between claimants who require or desire consumer protection, and those who do not – as the Lehman example illustrates. For the reasons explained above, an opt-out system has advantages, in that it ensures that consumers who wish to take advantage of consumer protection laws are not automatically excluded because they meet threshold criteria which can never be a true gauge of sophistication.

Therefore, the best solution is likely to involve some sort of self-certification or third-party certification concerning the assets and income of the individual or business, and confirming their understanding of the protection that they will lose.

In the following chapter, I will address various risks of litigation funding, and regulatory options. In doing so, I will consider the possibility of tailored regulation.

Promoting a social good

Some regulation cannot be explained or justified in economic terms.²⁷ The second reason or justification for regulation is that it furthers some social good. So, for example, regulating to protect the environment might be considered to be in the public interest, even if its economic consequences were neutral or negative.

In the context of litigation funding, regulation might be desirable to protect or further several social goods. First, it might be thought desirable to protect vulnerable claimants (separately from any economic benefit of doing so). Secondly, it might be thought desirable to protect defendants, and the court system, from the externalities which litigation funding might cause (again, separately from the economic benefit of doing so). Thirdly, it might be desirable to protect the integrity of the legal profession, in order to protect confidence in the justice system. This topic is addressed in Chapter 11.

I explained in Chapter 3 the critical role that the civil justice system plays in society, and in promoting the rule of law. There are economic benefits in complying with the rule of law. But even if there were not, the legal system is a critical public good, which deserves protection. Protecting the legal profession is therefore critically important as a social good.

²⁷ Eg Arthur Allen Leff, 'Economic Analysis of Law: Some Realism about Nominalism' (1974) 60 *Virginia Law Review* 451; Tony Prosser, 'Public Service Law' (2000) 63 *Law and Contemporary Problems* 63, 72-5, 81-2; Mike Feintuck, *The Public Interest in Regulation* (Oxford University Press 2004 (reprinted 2007)), Chapters 3 to 5 (and the literature there discussed); Tony Prosser, 'Regulation and Social Solidarity' (2006) 33 *Journal of Law and Society* 364; Feintuck (n 1) 43-4, 51-2; Baldwin (n 4) 22-3 (and the literature there cited).

Is regulation really necessary?

There are two broad reasons why governments in England and Australia regulate: to correct a market failure, or to promote some other social purpose or public interest.²⁸ Further regulation of the litigation funding industry might therefore be justified as being necessary to correct the market failures described in this chapter. It might also be justified if such regulation were to protect the public interest – for example, by preventing adverse consequences to claimants and defendants, and for the smooth operation of the civil justice system.

There are, however, powerful arguments against further regulation at the present time. First, even where a market failure exists, it may not be economically desirable to correct it if the cost of correcting the failure exceeds the cost of the failure.²⁹ Secondly, although this chapter has identified some important risks of litigation funding, evidence about their frequency and likelihood in practice is still emerging, and is piecemeal.³⁰ Thirdly, unnecessarily ‘heavy-handed’ regulation could lead to the undesirable consequence of satellite litigation.³¹ Some of these risks have also received relatively little attention to date in the academic literature – such as information asymmetry, and its consequences. The magnitude and likelihood of any risks are relevant to developing specific proposals, because they might affect matters such as the form of regulation.

²⁸ HM Treasury, *The Green Book: Central Government Guidance on Appraisal and Evaluation* (2018), [2.4]; Australian Government, *Australian Government Guide to Regulatory Impact Analysis* (2020), 21.

²⁹ See, eg, Veljanovski (n 2) 22-3.

³⁰ The absence of evidence of problems in practice led to the current regime of ‘light-touch’ regulation in Australia: Wayne Attrill, ‘The Regulation of Conflicts of Interest in Australian Litigation Funding’ (UNSW Class Actions: Securities and Investor Cases Seminar, Sydney, 29 August 2013), 1-2.

³¹ Rachael Mulheron and Peter Cashman, ‘Third Party Funding: A Changing Landscape’ (2008) 27 *Civil Justice Quarterly* 312, 321.

On the other hand, regulation may be desirable for standard-setting, particularly given the novelty of the industry, and uncertainties about the application of existing law to funding agreements. It could also be said that the participation of litigation funders in the civil justice system justifies regulation in any event. By comparison, barristers are subject to extensive professional standards in order to protect confidence in the civil justice system. For example, barristers in England are prohibited from referring to their professional status in private disputes. This rule does not address any market failure. Further, there is no suggestion that, in the absence of the rule, there would be widespread abuses. Rather, the purpose of the rule is to avoid bringing the profession into disrepute, which is, in turn, thought necessary to maintain public confidence in the civil justice system. The rule is essentially prophylactic. It also serves to set a standard and/or reinforce a value of the profession. Further, as will be discussed in the following chapters, there is evidence that some of the market failures which have been identified in this chapter are occurring in practice.

In the case of litigation funding, it is arguable that regulation might serve to set standards, and to set out values or boundaries for the industry. Further, such regulation might maintain or promote confidence in the civil justice system.

Conclusion

I commenced this chapter by introducing the concept of market failures, and explaining why they provide a basis for regulating markets. I then explained what the market failures are in the litigation funding market.

In the following chapter, I consider the existing state of the regulation of litigation funding.

CHAPTER 9: THE EXISTING REGULATION OF LITIGATION FUNDING

Introduction

In this chapter, I identify the existing law applying to litigation funding. It will be seen that the primary restrictions are imposed by judicial regulation, and voluntary codes. I will explain that the current arrangements are unsatisfactory: judicial regulation is inherently piecemeal and retrospective, and voluntary codes are obviously limited in their effect.

Self-regulation

Self-regulation is well-established in the English funding industry. The Civil Justice Council working party on third party funding drafted a voluntary code as early as 2008.¹ In his Final Report following from his Review of Civil Litigation Costs, Lord Justice Jackson made some recommendations for how the code might be amended.² The code was revised in response,³ and the Association of Litigation Funders (‘the ALF’) was established in 2011.⁴ Members of the ALF are required to comply with the Code of Conduct as a condition of membership.⁵ Whilst not giving blanket endorsement to the Code of Conduct as a whole, courts have treated aspects as indicating the demands of

¹ Civil Justice Council, ‘Third Party Funding’ (*Courts and Tribunals Judiciary*,) <<https://www.judiciary.uk/related-offices-and-bodies/advisory-bodies/cjc/archive/costs-funding-and-third-party-funding/third-party-funding-2/>> accessed 3 August 2020.

² Lord Justice Rupert Jackson, *Review of Civil Litigation Costs: Final Report* (2009), Chapter 11, [2.3]-[2.12].

³ Civil Justice Council (n 1).

⁴ Association of Litigation Funders, ‘Our Founding’ <<http://associationoflitigationfunders.com/about-us/our-founding/>> accessed 2 July 2019.

⁵ Association of Litigation Funders, *Rules of the Association* (2016), rules 3.4, 3.15 and 6.1.

responsible practice, and seem to treat ALF membership as an indicator of a reputable funder.⁶ However, not all funders are members of the Association.

The Code provides that a funder's 'promotional material... must be clear and not misleading'.⁷ A funder must 'take reasonable steps' to ensure that the claimant has obtained 'independent advice' on the funding agreement before execution, which is satisfied if the lawyer acting in the matter provides such advice.⁸

The Code requires that all funding agreements contain terms as to whether or not the funder will assume liability for adverse costs, after-the-event insurance, securities for costs and other liabilities, but is not prescriptive as to the content of any such terms.⁹

The Code prescribes certain features of a litigation funding agreement. In relation to the issue of control, the Code prohibits funders from conduct which is likely to cause the client's lawyers to breach their professional obligations, or 'seek[ing] to influence [the lawyers]... to cede control or conduct of the dispute to the Funder'.¹⁰ Further, the funding agreement must state whether and how the funder may 'provide input' into decisions about settlement.¹¹ But the Code expressly preserves the right of a funder to conduct 'appropriate due diligence', including during the litigation process,

⁶ *Excalibur Ventures LLC v Texas Keystone Inc* [2016] EWCA Civ 1144; [2016] 6 Costs LO 999, [30]-[31], cf [27]; *Akhmedova v Akhmedov* [2020] EWHC 1526 (Fam), [44]-[45].

⁷ Association of Litigation Funders, *Code of Conduct for Litigation Funders* (2018), [6].

⁸ *ibid* [9.1].

⁹ *ibid* [10].

¹⁰ *ibid* [9.2], [9.3].

¹¹ *ibid* [11.1].

which may entail ‘analysis of the law, facts, witnesses and costs relating to a claim... including regularly reviewing the progress of the litigation’.¹²

The Code precludes the funder from having a general discretionary right to terminate the funding agreement.¹³ Funders may only have rights of termination in circumstances where they *reasonably* ‘cease[] to be satisfied about the merits of the dispute’, or believe it to be ‘no longer commercially viable’, or believe ‘that there has been a material breach’ of the agreement by the claimant.¹⁴ The funder remains liable for accrued funding obligations as at the date of termination, ‘unless the termination is due to a material breach’.¹⁵

If disputes do arise concerning settlement or termination, ‘a binding opinion shall be obtained from a Queen’s Counsel who shall be instructed jointly or nominated by the Chairman of the Bar Council.’¹⁶ The Code also provides that the Association will ‘maintain a complaints procedure’, to which the funder must submit.¹⁷

The Code, and the Rules of the Association, are relatively prescriptive concerning capital adequacy requirements. In addition to a general duty to maintain ‘access to adequate financial resources to meet [its] obligations’,¹⁸ there are specific requirements to maintain sufficient capital to satisfy funding obligations for three years,¹⁹ and to maintain £5 million of capital in any event.²⁰ ‘Exposure’ must be

¹² *ibid* [18]. This provision appears to have been added in response to the *Excalibur* judgment, discussed in Chapter 10.

¹³ *ibid* [12].

¹⁴ *ibid* [11.2].

¹⁵ *ibid* [13.1].

¹⁶ *ibid* [13.2].

¹⁷ *ibid* [15].

¹⁸ *ibid* [9.4].

¹⁹ *ibid* [9.4.1.2].

²⁰ *ibid* [9.4.2]; ALF, *Rules of the Association* (n 5) [3.15.1].

assessed at the time of making a new funding commitment, and monthly thereafter; the Rules provide that funders must be ‘conservative in assessing what is counted as capital’, and ‘pessimistic’ about predicted future returns from existing funding agreements.²¹ Funders must also provide the Association annually with an audit opinion as to their financial position (amongst other requirements).²²

The capital requirement of £5 million applies irrespective of the size of the funder and the extent of its obligations. There might be a risk that this figure could create a barrier to entry for new funders.²³

A funder’s obligation to maintain capital reserves extends to ensuring that its ‘Funder Subsidiaries’ and ‘Associated Entities’ also maintain necessary reserves.²⁴ This is consistent with the broader scheme of the Code, which identifies the funder as the entity that accepts responsibility towards the ALF,²⁵ but recognises that it may be another entity in the corporate group that enters the funding agreement,²⁶ or holds the funds.²⁷ The potential difficulty, however, is that even if the funding agreement establishes some contractual obligation to the claimant to maintain capital adequacy, it may be owed by a different entity to that which has capital adequacy obligations under

²¹ ALF, *Rules of the Association* (n 5) [3.15.5]-[3.15.6].

²² ALF, *Code of Conduct* (n 7) [9.4.4]; *ibid* [3.15.2]-[3.15.4].

²³ Timothy Lou, ‘Into the Shadows: Shadow Banking and the Prudential Regulation of Litigation Funders’ (2014) 14 *Macquarie Law Journal* 73, 86. However, Lou is incorrect to say that this requirement will be insufficient to regulate large funders: funders must also satisfy the requirement to maintain sufficient capital for three years’ worth of funding obligations. In effect, therefore, there are alternative capital requirements, and in practice the minimum capital requirement will be calculated by reference to the three-years rule for some, and the £5 million minimum rule for others.

²⁴ ALF, *Code of Conduct* (n 7) [9.4].

²⁵ *ibid* [4].

²⁶ *ibid* [5.2].

²⁷ *ibid* [2.1], [2.2].

the Code.²⁸ Further, the Code makes clear in any event that a funder's obligations to comply with the Code (including its capital adequacy obligations) are owed to the ALF, and not to the client,²⁹ so that in the absence of a contractual provision, a claimant cannot insist on any particular arrangements concerning capital. However, these difficulties are mitigated by the funder's obligation to inform the claimant of the identity of the counterparty to the funding agreement (i.e. whether it is the funder or another member of the corporate group),³⁰ and the commercial reality that a funder who acts as the public-facing entity, and has chosen to take on the obligations (and imprimatur) of ALF regulation, has incentive to ensure that other members of its corporate group are appropriately capitalised.

In endorsing the concept of self-regulation, Lord Justice Jackson nevertheless offered the following words of qualification:³¹

Provided that a satisfactory code is established and that all funders subscribe to that code, then at this stage... I see no need for statutory regulation. However, if the use of third party funding expands, there may well be a need for full statutory regulation.

As to the general utility of self-regulation, five points arise. First, not all funders subscribe to the code. There are currently nine funder members of the ALF. It is likely that making the self-regulatory scheme compulsory – either directly, or indirectly (for example, by requiring solicitors to deal only with ALF members) – would be impermissible as being anti-competitive, in the absence of any statutory underpinning for such an obligation.³² Secondly, one funder member has collapsed, in circumstances

²⁸ Rachael Mulheron, 'England's Unique Approach to the Self-Regulation of Third Party Funding: A Critical Analysis of Recent Developments' (2014) 73 *Cambridge Law Journal* 570, 576-7.

²⁹ ALF, *Code of Conduct* (n 7) [4]; *ibid* 577.

³⁰ ALF, *Code of Conduct* (n 7) [5].

³¹ Jackson (n 2) Chapter 11, [2.12].

³² Mulheron (n 28) 579.

which involved allegations of dishonesty.³³ Thirdly, the *Excalibur* litigation provided a high-profile example of an inexperienced funder, who was not a member of the ALF, funding, and failing to supervise appropriately, litigation which went seriously awry. Fourthly, the industry has expanded very substantially since Lord Justice Jackson made those remarks in 2009.³⁴ Accordingly, one might well question whether the time is ripe for statutory regulation of funding.³⁵ Finally, self-regulation must be, in some respects, inherently limited in its ambition; for example, it would not be open to the ALF to regulate in a manner which was inconsistent with the common law position on the extent of permissible funder control, and an industry body such as the ALF does not have available to it the resources of the state to police and enforce standards.

As to the content of the ALF Code, it is most comprehensive in dealing with capital adequacy and rights of termination. In relation to control, it probably adds little to the common law position. Secondly, it does not purport to address all market failures described in the previous chapter (and nor could it) – for example, it does not make any prescription concerning the issue of liability for adverse costs, which includes an externality.

In Australia, self-regulation is in an embryonic stage. The Association of Litigation Funders of Australia ('the ALFA') was established in April 2018,³⁶ and

³³ The funder was Argentum; this is discussed further in Chapter 10.

³⁴ See Chapter 6.

³⁵ Indeed, Lord Justice Jackson himself indicated that statutory regulation might be necessary if the industry expanded, or was used for group actions by consumers, both of which have occurred: see Jackson (n 2) Chapter 11, [2.4], [2.12], [3.4].

³⁶ Association of Litigation Funders of Australia, 'Association of Litigation Funders Australia - News' <<https://www.associationoflitigationfunders.com.au/news.html>> accessed 28 June 2019.

presently has 11 members.³⁷ In January 2019, it published Best Practice Guidelines for Litigation Funders and Managers ('the ALFA Guidelines').³⁸ The ALFA Guidelines are not compulsory for members; rather, they are intended to 'represent a best practice framework within which Members may develop their own standards, policies and procedures'.³⁹ Insofar as members do not follow the ALFA Guidelines, they are expected to inform potential claimants of that fact.⁴⁰

In many respects the ALFA Guidelines echo (if not replicate) the ALF Code, although there are four notable deviations. First, members are not prevented from seeking to exert control over litigation.⁴¹ Secondly, whilst there is a requirement to maintain adequate financial resources,⁴² there is no indication of what is to be regarded as 'adequate'.⁴³ Thirdly, members are expected to maintain a complaints procedure, rather than (as in the ALF Code) being required to subscribe to the Association's complaints procedure.⁴⁴ Fourthly, there is no provision dealing with membership of a corporate group.⁴⁵

³⁷ Association of Litigation Funders of Australia, 'Home Page' <<https://www.associationoflitigationfunders.com.au/>> accessed 28 June 2019. Omni Bridgeway, Australia's largest funder, is a notable omission from the list of members.

³⁸ Association of Litigation Funders of Australia, *Best Practice Guidelines for Litigation Funders & Managers* (2019).

³⁹ *ibid* [1].

⁴⁰ *ibid* [2].

⁴¹ i.e., there is no equivalent to [9.3] of the ALF Code of Conduct.

⁴² ALFA, *Guidelines* (n 38) [10].

⁴³ i.e., there is no equivalent to [9.4] of the ALF Code of Conduct.

⁴⁴ ALFA, *Guidelines* (n 38) [15], and compare ALF, *Code of Conduct* (n 7) [15].

⁴⁵ Discussed above in the text accompanying footnotes 24 to 30.

Externally-imposed regulation

In England, there is no externally-imposed regulation of the funding industry. There is, in Australia, some very limited regulation of litigation funding, via the Corporations Regulations. The Australian regulation has developed in a manner which is largely adventitious. The background may be briefly summarised.

In a series of judgments between 2009 and 2012, various Australian courts considered whether certain laws which regulated the financial services market were applicable to litigation funding. In 2009, the Full Federal Court held that the funding agreements in a class action were a ‘managed investment’ within the meaning of the *Corporations Act*,⁴⁶ and therefore subject to the extensive regulations designed to protect the interests of investors.⁴⁷ Then in 2011, the New South Wales Court of Appeal held that the services provided by litigation funders were such that funders required an Australian Financial Services Licence (AFSL) to operate in Australia.⁴⁸ Entities which hold an AFSL are also subject to specific regulations, including general obligations to maintain ‘adequate arrangements’ for managing conflicts of interest, to provide certain information to the Australian Securities and Investments Commission (ASIC),⁴⁹ and to provide services ‘efficiently, honestly and fairly.’⁵⁰ For retail clients, there are also

⁴⁶ *Brookfield Multiplex Ltd v International Litigation Partners Pte Ltd* [2009] FCAFC 147; (2009) 180 FCR 11. Managed investment schemes are a form of collective investment, commonly used by small investors as an alternative to direct investment in the share market.

⁴⁷ Corporations Act 2001 (Cth), Part 5C; *ibid* [2]-[32], especially [31]-[32] (Sundberg and Dowsett JJ); [123]-[158] (Jacobson J).

⁴⁸ *International Litigation Partners Pte Ltd v Chameleon Mining NL* [2011] NSWCA 50; (2011) 82 ACSR 517.

⁴⁹ ASIC is ‘Australia’s corporate, markets and financial services regulator’: ‘About ASIC’ <<https://asic.gov.au/about-asic>> accessed 7 September 2020.

⁵⁰ See generally Corporations Act 2001 (Cth), Part 7.6.

obligations to maintain dispute resolution procedures and compensation arrangements.⁵¹

This judgment was overturned on appeal to the High Court of Australia, where the majority concluded that the litigation funding agreement in question was a ‘credit facility’ for the purposes of the *Corporations Act*.⁵² Whilst this meant that there was no obligation for the funder to hold an AFSL, it would have meant that funders would be required to comply with yet another form of financial regulation, the *National Credit Code*.⁵³ Again, this imposes particular regulatory requirements on those who provide credit facilities, including a licensing regime,⁵⁴ obligations concerning maintenance of financial records,⁵⁵ and extensive requirements concerning the entry into and content of credit agreements.⁵⁶

Had any of these judgments stood, the effect would have been to impose very onerous consumer protection obligations on litigation funders.

⁵¹ See generally *ibid* ss 912A-912F as to the obligations.

⁵² *International Litigation Partners Pte Ltd v Chameleon Mining NL (Receivers and Managers Appointed)* [2012] HCA 45; (2012) 246 CLR 455, [15], [17], [18], [33] (French CJ, Gummow, Crennan and Bell JJ).

⁵³ National Consumer Credit Protection Act 2009 (Cth), Schedule 1. As to the applicability of the Act following the High Court’s judgment, see ASIC, *ASIC extends relief from regulation for all funded representative actions and funded proof of debt arrangements* (2013); cf Michael Duffy, ‘Two’s Company, Three’s a Crowd? Regulating Third-Party Litigation Funding, Claimant Protection in the Tripartite Contract, and the Lens of Theory’ (2016) 39 *University of New South Wales Law Journal* 165, 180.

⁵⁴ National Consumer Credit Protection Act 2009 (Cth), Part 2-2.

⁵⁵ *ibid* Part 2-5.

⁵⁶ *ibid* Schedule 1 – *National Credit Code*.

But the results were reversed in two ways.⁵⁷ First, ASIC issued successive class orders which had the effect of exempting litigation funders from the obligations which were imposed by the successive judgments.⁵⁸

Secondly, in 2012, the *Corporations Regulations* ('the Regulations') were amended, with a view to making more stable arrangements.⁵⁹ Those regulations exempted funders from the broader financial services regulation which the judgments had imposed.⁶⁰ However, the Regulations impose certain requirements for managing conflicts of interest. The obligations imposed by the Regulations have been supplemented quite extensively by regulatory guidance issued by the Australian Securities and Investment Commission ('the Regulatory Guide').⁶¹

⁵⁷ See generally Australian Government Productivity Commission, *Access to Justice Arrangements (Productivity Commission Inquiry Report No 72)* (2014), 610.

⁵⁸ ASIC Class Order [CO 10/333]; ASIC Class Order [CO 13/18] - Funded representative proceedings and funded proof of debt arrangements exclusion from the National Consumer Credit Protection Act 2009. See also ASIC, *ASIC Grants Transitional Relief from Regulation for Funded Class Actions* (2009), ASIC, *ASIC Grants Interim Class Order Relief from Regulation for all Funded Representative Actions and Funded Proof of Debt Arrangements* (2010), ASIC, 'ASIC Extends Relief from Regulation' (n 53).

⁵⁹ See generally Australian Securities and Investment Commission, *Litigation Schemes and Proof of Debt Schemes: Managing Conflicts of Interest (Regulatory Guide 248)* (2013) for ASIC's guidance as to the operation of the Regulations. Note, however, that some content in ASIC's guidance must be regarded as matters of 'best practice', rather than a strict requirement imposed by the regulations.

⁶⁰ First, the Regulations provide that litigation funding 'schemes' and 'arrangements' fall outside the definition of managed investment scheme in the Corporations Act: Corporations Regulations 2001 (Cth), reg 5C.11.01(1)(b)-(d). In short, the definition of a 'scheme' captured class actions, or proceedings brought by external administrators which are funded by the creditors: reg 5C.11.01(1)(b) and (c); ASIC, *Regulatory Guide* (n 59) RG 248.2 and 248.4. The definition of an 'arrangement' captured individual funding agreements: reg 5C.11.01(1)(d); ASIC, *Regulatory Guide* (n 59) RG 248.3. Thus, all litigation funding agreements were excluded from the definition of managed investment scheme, and thus from the regulation applicable to managed investment schemes.

The Regulations also specified that although litigation funding schemes and arrangements are financial products (reg 7.1.04N), they are not credit facilities for the purposes of the Corporations Act: reg 7.1.06(2A) and (2B). This may mean that the National Credit Code does not apply. Finally, the Regulations confirmed that litigation funding schemes and arrangements were exempt from the requirement to hold an AFSL: reg 7.6.01(1)(x) and (y).

⁶¹ Wayne Attrill, 'The Regulation of Conflicts of Interest in Australian Litigation Funding' (UNSW Class Actions: Securities and Investor Cases Seminar, Sydney, 29 August 2013), 4, observes (correctly) that in its Guidance, 'ASIC has put (rather a lot of) flesh on the bones of the regulations'.

The requirements apply to those who are providing *financial* services for a litigation funding scheme or arrangement.⁶² This means that the Regulations are usually applicable only to the funder, and not to the lawyer.⁶³

The funder's obligation is to maintain and follow 'adequate practices for managing any conflict of interest that may arise in relation to activities undertaken by the person, or an agent of the person, in relation to the scheme or arrangement'.⁶⁴ The Regulations do not prescribe how conflicts of interest must be resolved, but provide that the funder (described as 'the person') will have adequate practices if they can 'show through documentation' that various requirements have been satisfied. First, they must have reviewed their business operations to identify potential conflicts of interest.⁶⁵ Secondly, they must have written and implemented procedures for managing conflicts, which are reviewed at least annually.⁶⁶ Thirdly, compliance with these regulations must be 'implemented, monitored and managed' by a sufficiently senior officer of the funder.⁶⁷

The written procedures must deal with specific topics, including 'managing situations in which interests may conflict', and how to deal with pre-existing relationships between funder, claimant and lawyer, but no guidance is given as to how they are to be resolved.⁶⁸

⁶² Corporations Regulations 2001 (Cth), reg 7.6.01AB(2).

⁶³ ASIC, *Regulatory Guide* (n 59) RG 248.9 and RG 248.10; see also Attrill (n 61) 10-11.

⁶⁴ Corporations Regulations 2001 (Cth), reg 7.6.01AB(2).

⁶⁵ *ibid* 7.6.01AB(4)(a).

⁶⁶ Corporations Regulations 2001 (Cth), 7.6.01AB(4)(b); ASIC, *Regulatory Guide* (n 59) RG 248.28-44 and RG 248.52.

⁶⁷ Corporations Regulations 2001 (Cth), 7.6.01AB(4)(f); ASIC, *Regulatory Guide* (n 59) RG 248.45-47.

⁶⁸ Corporations Regulations 2001 (Cth), 7.6.01AB(4)(d).

Finally, the terms of any funding agreement must be ‘reviewed to ensure the terms are consistent with Division 2 of Part 2 of the *Australian Securities and Investments Commission Act 2001*’.⁶⁹ This requirement is unclear in several respects. Division 2 of Part 2 of the ASIC Act contains various consumer protections, including the prevention of unfair contract terms, and the prohibition against misleading or deceptive conduct and unconscionable conduct (in various forms). However, on its face, the ASIC Act is limited to consumer contracts. It is unclear, therefore, whether the obligation to ensure that the terms of funding agreements are consistent with the ASIC Act (1) is limited to funding agreements which are *also* consumer contracts, or (2) extends to *all* funding agreements, even those which would not otherwise fall within the ambit of the ASIC Act. Further, it seems on the face of the Regulations that only the unfair contract terms of the ASIC Act are imported. But the Regulatory Guide suggests otherwise.⁷⁰ It is therefore unclear which obligations are imported from the ASIC Act.

Finally, there is a very important and overlooked difficulty in identifying the scope of the Regulations and Regulatory Guide. On their face, the Regulations purport to apply to all litigation funding agreements.⁷¹ But the Regulatory Guide – which ‘put[s] (rather a lot of) flesh on the bones of the regulations’⁷² – is predominantly concerned with class action funding agreements. For example, the Regulatory Guide identifies a particular concern about conflicts of interest at the point of settlement, but then states that sufficient protection is provided by the court approval process where

⁶⁹ *ibid* reg 7.6.01AB(4)(e).

⁷⁰ See the next footnote.

⁷¹ The Regulatory Guide refers throughout to ‘litigation schemes’. However, confusingly, an annex to the Regulatory Guide states that for the purpose of the Guide, a ‘litigation scheme’ means ‘A scheme... or an arrangement’: ASIC, *Regulatory Guide* (n 59) Key Terms, 28.

⁷² Attrill (n 61) 4.

there is a class action.⁷³ But, of course, settlements need not be approved outside the class action context. It is not clear, therefore, whether the Regulatory Guide is intended to apply outside a class action context.

In summary, the following matters are either not dealt with in the Regulations or Regulatory Guide, or are dealt with in an unsatisfactory manner:

- There is no guidance for how conflicts of interest are to be managed. In particular, there is a serious omission of any treatment of conflicts of interest at the point of settlement.
- It is not clear whether the consumer protections offered by the ASIC Act apply to all funding agreements, or just to those which would be captured by the ASIC Act in any event.
- The Regulations and Guidelines regulate only funders, and not lawyers.
- It is not clear whether the Regulatory Guidance is in fact intended to operate outside the class action context.
- Several important issues are not dealt with at all. These include issues of capital adequacy, and disclosure at the time of entry into the funding agreement.

Regulation in this area continues to evolve, as will be explained later.

Judicial regulation of litigation funding

Owing to various lacunae in the regulation of litigation funding, courts have been required to resolve some of the issues which funding has presented. Obviously, the

⁷³ ASIC, *Regulatory Guide* (n 59) RG248.89, RG248.90.

scope of permissible funding agreements is still constrained by the doctrines of maintenance and champerty. The present state of those doctrines was addressed in Chapter 2.

In Australia, judicial regulation is evident in three areas: the use of litigation funding in class actions, its use by insolvency practitioners, and the question of security for costs. In England, judicial regulation has focused on the circumstances in which a funder will be required to pay the adverse costs of a successful defendant. These will be considered in turn. I will then identify the problems of judicial regulation.

Judicial regulation of class action funding

It will be recalled from Chapter 6 that litigation funding has been critical to the development of class actions in Australia, owing to the onerous cost obligations placed on the representative claimant and the absence of any provision in the Federal Court Act to address costs, or to establish a common fund for class actions. Whilst some other Australian jurisdictions have now introduced class actions, Part IVA claims in the Federal Court are the dominant form of Australian class action.

In order for funding to be commercial in a class action, funders first developed the technique of the ‘closed class’ – that is, the class would be defined as comprising a group of claimants who had suffered an identifiable form of loss, *and* had entered into a funding agreement with the funder.⁷⁴ From the perspective of the funder, closed classes have the advantage of certainty: the funder knows what the percentage funding commission will be, and knows how many group members will pay that commission.⁷⁵

⁷⁴ Endorsed in *Multiplex Funds Management Ltd v P Dawson Nominees Pty Ltd* [2007] FCAFC 200; (2007) 164 FCR 275.

⁷⁵ *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148; (2016) 245 FCR 191, [190].

The use of closed classes posed several problems, however. First, the potential for competing classes is obvious. If a closed class is defined by reference to claimants who have entered into a litigation funding agreement with Funder A, then it is open to Funder B to commence a second Part IVA action, where the closed class is defined by reference to a different group of claimants.⁷⁶ There is no procedural mechanism for dealing with competing classes in the Act. Competing classes have an obvious tendency to lead to wasteful expenditure of the parties and court's resources, and are also onerous for the defendant.⁷⁷ The problem is even more acute if the class actions are commenced in different Australian jurisdictions. The Federal Court has recognised that, faced with competing Part IVA actions, there are a variety of potential solutions, none of which will be suitable for all circumstances.⁷⁸

Secondly, it has been argued persuasively that the use of closed classes is inconsistent with the policy reasons which led to the decision to make Part IVA actions opt-out.⁷⁹

Thirdly, as a practical matter, a litigation funder must enter into agreements with a sufficient number of potential claimants in order to achieve a critical mass, and make the litigation economic.⁸⁰ The process of recruiting class action claimants is known as

⁷⁶ Susanna Khouri, Wayne Attrill and Clive Bowman, 'Litigation Funding and Class Actions - Idealism, Pragmatism and a New Paradigm' in Damian Grave and Helen Mould (eds), *25 Years of Class Actions in Australia, 1992-2017* (Herbert Smith Freehills 2017), 248.

⁷⁷ *Money Max* (n 75) [196]; see also *Perera v GetSwift Limited* [2018] FCAFC 202; (2018) 363 ALR 394, [122].

⁷⁸ Australian Law Reform Commission, *Integrity, Fairness and Efficiency—An Inquiry into Class Action Proceedings and Third-Party Litigation Funders (ALRC Report 134)* (2018) [4.58]-[4.62].

⁷⁹ See Rachael Mulheron, 'Third Party Funding and Class Actions Reform' (2015) 131 Law Quarterly Review 291, 305-7; See, eg, *Multiplex* (n 74) [117], and generally [108]-[117] (Jacobson J, French J agreeing); see also *Money Max* (n 75) [193], *Blairgowrie Trading Ltd v Allco Finance Group Ltd (Receivers & Managers Appointed) (In Liq)* [2015] FCA 811; (2015) 108 ACSR 1, [225].

⁸⁰ *Money Max* (n 75) [186]; *Allco* (n 79) [27].

book building. It involves identifying potential claimants, notifying them about the proposed claim, and encouraging them to enter a retainer and funding agreement.⁸¹

This bookbuild process may be costly, and these costs will ultimately be borne by funded claimants.

The difficulties caused by closed classes⁸² were, in turn, addressed through judicial regulation. A substantial and growing body of Federal Court jurisprudence sought to encourage ‘open classes’ – that is, classes which capture all injured parties, and not just the subset who have signed a funding agreement – even in funded matters.

First, sanction was given to the use of ‘funding equalisation orders’ (‘FEO’). These may be made where the class action has an ‘open class’; that is, the class comprises both funded and unfunded claimants. Only the funded claimants have an obligation to pay a percentage of their recovery to the funder. However, an FEO has the effect of requiring deductions to be made from the recovery of the unfunded claimants, which are then distributed across the whole class. By this technique, the costs of funding are shared by every claimant.⁸³ It does not affect the quantum of the funder’s return – the funder still receives an amount equal to X% of the recovery of the funded litigants. But the source of the funder’s return changes – it is paid by all litigants, and not just those who entered the funding agreement.

⁸¹ John Walker, Susanna Khouri and Wayne Attrill, ‘Funding Criteria for Class Actions’ (2009) 32 UNSW Law Journal 1036, 1044.

⁸² Note, however, that Morabito presents compelling arguments as to the desirability of closed classes in some cases: Vince Morabito, *An Evidence-Based Approach to Class Action Reform in Australia: Closed Class Actions, Open Class Actions and Access to Justice* (2018).

⁸³ Explained by Full Court in *Money Max* (n 75) [5] (and see also [130]-[132]), and by Wigney J in *Allco* (n 79) [164] (and see his Honour’s further comments at [188], [226]).

Secondly, in *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* (*‘Money Max’*),⁸⁴ the Full Court sanctioned the making of a ‘common fund order’ (‘CFO’) at the *start* of proceedings.⁸⁵ A CFO has the effect that all group members (in an open class) contribute an equal percentage of any judgment or settlement towards the payment of legal costs and the funding commission. The percentage would be determined by the Court at the conclusion of the proceedings, taking into account matters including the likely return by class members, and market rates.⁸⁶ The utility of making such an order at the start of proceedings, though, is to provide some commercial certainty to the funder as to its likely return. The Full Court found that it had power to make such an order under s 33ZF(1) of the *Federal Court Act*, which provides

In any proceeding ... conducted under this Part, the Court may, of its own motion or on application by a party or a group member, make any order the Court thinks appropriate or necessary to ensure that justice is done in the proceeding.

But the court’s encouragement of open classes, in turn, added a further nuance to the question of what to do about competing classes. Contrary to some predictions,⁸⁷ CFOs led to an *increase* in competing class actions.⁸⁸ This is because funders no longer needed to conduct a book-build.⁸⁹

⁸⁴ n 75.

⁸⁵ I discuss common fund orders in detail (and funding equalisation orders to a lesser degree) in Stefanie Wilkins, ‘Common Fund Orders in Australia: A New Step in Court Regulation of Litigation Funding: *Money Max Int Pty Ltd (Trustee) v QBE Insurance Group Limited* [2016] FCAFC 148’ (2017) 36 *Civil Justice Quarterly* 133.

⁸⁶ *Money Max* (n 75) [80].

⁸⁷ Jason Betts, David Taylor and Christine Tran, ‘Litigation Funding for Class Actions’ in Damian; Mould Grave, Helen (ed), *25 years of Class Actions in Australia, 1992-2017* (Herbert Smith Freehills 2017), 215.

⁸⁸ ALRC, *Integrity, Fairness and Efficiency* (n 78) [4.32] (referring to several submissions which were made to that effect); *Perera* (Full Court) (n 77) [159].

⁸⁹ ALRC, *Integrity, Fairness and Efficiency* (n 78) [4.32]-[4.33].

The Full Federal Court again adopted a regulatory function, and developed principles about what to do about competing open classes. In *Perera v Getswift Ltd*,⁹⁰ the Full Court considered that this involved an exercise of discretion in the circumstances of the case, and identified the criteria for the exercise of this discretion.⁹¹ The Court was of the view that lower costs of funding ought not to be given undue weight, to avoid a ‘rush to the bottom’, which they considered was already evident to some extent in the market.⁹² Rather, in circumstances where the court had the power to supervise funding and legal costs at the state of settlement approval:⁹³

... the Court should focus less on achieving the lowest possible costs and funding charges in any selection process, and more on selecting the proceeding with a funding and costs models likely to best motivate the applicant’s solicitor and funder to work assiduously to achieve the best outcome for the applicant and group members and to take responsible risks in that regard.

Further, the court should select the ‘most experienced and capable’ legal team where this was a ground of distinction, because this was most likely to achieve the best result for claimants.⁹⁴ Thirdly, the court should avoid encouraging a ‘rush to the Court’, by giving any advantage to those first to file (who would also be likely to be first to bookbuild).⁹⁵

The court accepted that the selection process which it had undertaken had two significant disadvantages. First, it provided the respondent with knowledge of the ‘war chest’ it would face, enabling deep-pocketing, and also enabling the respondent to know

⁹⁰ *Perera* (Full Court) (n 77).

⁹¹ *ibid* [273]-[282].

⁹² *ibid* [276].

⁹³ *ibid* [277].

⁹⁴ *ibid* [278].

⁹⁵ *ibid* [279].

when the costs limit was being approached, which might disincentivise solicitors to work, and lead funders to be more eager to settle.⁹⁶ Secondly, the selection process itself was expensive. Such costs had the potential to deter funders and/or solicitors, with the potential result of reducing competing and therefore increasing costs.⁹⁷

Again, the Federal Court assumed a regulatory function. Again, it determined that it had power to alter contractual relations. And, importantly, the Court assumed responsibility for selecting a funder.

Yet further issues have arisen where the competing class actions have been commenced in different jurisdictions.⁹⁸ This occurred in relation to a series of class actions commenced against AMP, a financial institution, where competing class actions and transfer applications were filed in the Federal Court and the New South Wales Supreme Court. The prospect of anti-suit injunctions being issued between Australian courts was regarded by both courts as being entirely antithetical to the comity required in the Australian federal system.⁹⁹ It provided the impetus for the Federal Court and the New South Wales Supreme Court to issue a joint protocol concerning the management of competing class actions filed in those jurisdictions.¹⁰⁰

The Federal Court has confirmed that it has power to reduce the funder's percentage in approving a settlement.¹⁰¹ In *Earglow*, Murphy J explained that such a

⁹⁶ *ibid* [281].

⁹⁷ *ibid* [282].

⁹⁸ In addition to the Federal Court, New South Wales, Victoria and Queensland each have a group litigation procedure.

⁹⁹ *Wigmans v AMP Limited* [2018] NSWSC 1118, [13]-[18]; *Wileypark Pty Ltd v AMP Limited* [2018] FCAFC 143, [10]-[13].

¹⁰⁰ Protocol for Communication and Cooperation between Supreme Court of New South Wales and Federal Court of Australia in Class Action Proceedings.

¹⁰¹ *Earglow Pty Ltd v Newcrest Mining Limited* [2016] FCA 1433, [7], [133]-[134], [157]. Cf *Mitic v OZ Minerals Limited (No 2)* [2017] FCA 409, [27]-[31] (Middleton J there disagreed as to the statutory source of the power).

power was enlivened where the funding commission was ‘excessive or disproportionate’.¹⁰² One of his Honour’s reasons for altering the terms of the contract was that small shareholders had had ‘limited’ choice in entering the funding agreement. Specifically,¹⁰³

It is likely that their only avenue to recover their alleged losses was through the proceeding, that they suffered a significant information asymmetry compared to the Funder in relation to the costs and risks the Funder assumed, and their opportunity for negotiation of the funding commission was limited or non-existent.

To here, the developments may be summarised as follows. The advent of litigation funding led to the development of the technique of ‘closed classes’, which were given judicial sanction as being permissible within the terms of the Act, but were generally regarded as being undesirable in some respects. Thus, the court, assuming a regulatory function, crafted solutions – FEOs and CFOs – to encourage the use of open classes in funded class actions. This, in turn, led to further litigation – and judicial regulation – concerning the criteria for selecting between competing classes. The court has also decreased funding commissions – thus altering the terms of concluded funding agreements – to address information asymmetry.

These developments alone demonstrate that judicial regulation of class action litigation funding has led to uncertainty and satellite litigation. This is inevitable, given that courts can only set down rules when called upon to do so by parties (necessitating satellite litigation) and do so by reference to events which have already occurred (which creates an element of uncertainty for funders wishing to plan their future activities). In its 2018 report, the ALRC recommended amendments to the Federal Court Act to

¹⁰² *Earglow* (n 101) [117]-[118].

¹⁰³ *ibid* [138] (citations omitted).

provide express powers to make CFOs and to resolve competing classes, in order to regularise the position.

This was a prescient recommendation: in December 2019 the High Court held that there was no power to make CFOs at the start of proceedings under s 33ZF(1),¹⁰⁴ thus setting aside three years of established law and practice which had developed in respect of the use of CFOs.

Even this is not the end. The Federal Court updated the practice note on class actions to provide that, particularly in open class actions, it may be expected that the court will¹⁰⁵

make an appropriately framed order to prevent unjust enrichment and equitably and fairly to distribute the burden of reasonable legal costs, fees and other expenses, including reasonable litigation funding charges or commission, amongst all persons who have benefited from the action.

Class members are to be informed of this early in the proceedings. Thus, the practice note confirms that the cost of funding may be distributed across the class at the *end* of proceedings, and that parties may expect this, notwithstanding that the order will *not* be made at the start. Subsequent judgments indicated that the Federal Court is likely to rely on the power under s 33V(2) to make an order distributing the cost of funding across the class at the end of proceedings,¹⁰⁶ and the first such order has now been made.¹⁰⁷ It is referred to as an Expense Sharing Order.¹⁰⁸

¹⁰⁴ *BMW Australia Ltd v Brewster* [2019] HCA 45.

¹⁰⁵ Federal Court of Australia, Class Actions Practice Note (GPN-CA), [15.4].

¹⁰⁶ *McKay Super Solutions Pty Ltd (Trustee) v Bellamy's Australia Ltd (No 3)* [2020] FCA 461, [31]; *Fisher (trustee for the Tramik Super Fund Trust) v Vocus Group Limited (No 2)* [2020] FCA 579, [68]-[72].

¹⁰⁷ *Uren v RMBL Investments Ltd (No 2)* [2020] FCA 647.

¹⁰⁸ *Lenthall v Westpac Banking Corporation (No 2)* [2020] FCA 423, [3].

There is a clear need for certainty and legislative reform in this area.¹⁰⁹ The complexity of the Australian case law, and the continued changes in approach, demonstrate well the inherent limitations of judicial regulation.

Practice notes

In those jurisdictions which have class action procedures (the Federal Court, New South Wales, Queensland and Victoria), the courts have created practice notes concerning their conduct of group proceedings. Most of these practice notes contain at least some provision dealing with litigation funding.

The most extensive provisions are to be found in the Federal Court. First, the representative claimant is required to disclose to the Court and other parties¹¹⁰

... any agreement by which a litigation funder is to pay or contribute to the costs of the proceeding, any security for costs or any adverse costs order and/or to receive payment of commission, costs or charges of any type in relation to the proceeding, whether by way of third-party or commercial litigation funding or by way of litigation funding provided by some of the class members.

There are equivalent provisions in New South Wales and Queensland.¹¹¹ The agreement may be disclosed in standard form, and disclosure need not be made of

¹⁰⁹ *McKay Super Solutions* (n 106) [33]-[34].

¹¹⁰ Federal Court of Australia, Class Actions Practice Note (GPN-CA), [6.1], [6.4], and see [5.1] as to the definition of 'litigation funding agreement'.

¹¹¹ Supreme Court of New South Wales, Practice Note SC GEN 17 – Supreme Court Representative Proceedings, [7.2]; Supreme Court of Queensland, Practice Direction Number 2 of 2017: Representative Proceedings, [8.2].

variations agreed with individual class members.¹¹² Sensitive terms may be redacted.¹¹³ Again, there are equivalent provisions in New South Wales and Queensland.¹¹⁴

The Federal Court Practice Note also contains various provisions regarding the content and form of litigation funding agreements. There is a requirement that such agreements be in writing,¹¹⁵ and obligations are placed on the representative claimant's lawyers concerning how class members are informed about the cost of funding.¹¹⁶ Any funding agreement must include provision for managing conflicts between any of the representative claimant, class claimants, the lawyers and any funder,¹¹⁷ and the lawyers have an obligation 'to recognise and to manage properly any conflicts throughout the proceeding'.¹¹⁸ In considering a proposed settlement, the court is empowered to supervise litigation funding charges.¹¹⁹ More onerous examination of funding is recommended where either (1) there is an open class; (2) 'the deduction per class member constitutes a significant proportion of the settlement amount otherwise payable to each class member'; (3), or the funder has imposed charges in a form other than a percentage (for example, by way of a 'project management fee').¹²⁰

¹¹² Federal Court of Australia, Class Actions Practice Note (GPN-CA), [6.4(a)].

¹¹³ Steven Friel and Jonathan Barnes (eds), *Litigation Funding 2019: Getting the Deal Through* (3rd edn, Law Business Research Ltd 2018), 13 and see also *Coffs Harbour City Council v Australian and New Zealand Banking Group Ltd (t/as ANZ Investment Bank)* [2016] FCA 306 as to examples of terms.

¹¹⁴ Supreme Court of New South Wales, Practice Note SC GEN 17 – Supreme Court Representative Proceedings, [7.2]; Supreme Court of Queensland, Practice Direction Number 2 of 2017: Representative Proceedings, [8.2].

¹¹⁵ Federal Court of Australia, Class Actions Practice Note (GPN-CA), [5.2].

¹¹⁶ *ibid* [5.3]-[5.5].

¹¹⁷ *ibid* [5.9].

¹¹⁸ *ibid* [5.10].

¹¹⁹ *ibid* [16].

¹²⁰ *ibid* [16.4].

Curiously, an identical provision appeared in earlier versions of the Victorian practice note on class actions,¹²¹ but it has been removed from the most recent version, issued in 2017.¹²² The Victorian Law Reform Commission, in its recent review of class actions and litigation funding, has recommended the inclusion of provisions similar to those found in the Federal Court practice note.¹²³

Proposals for reform

In September 2014, the Productivity Commission addressed third-party funding in its report on *Access to Justice Arrangements*.¹²⁴ The Commission expressed ‘support’ for third funding, but was concerned by the possibility of ‘abuses’ in the absence of regulation.¹²⁵ In relation to third-party funders, the specific concerns were:¹²⁶

- Agreements may be struck unfairly (for example, with excessive commissions) because consumers have limited capacity and experience compared to funders.
- Funders may exercise too much control over proceedings, and may place pressure on the court system.
- There are potential conflicts of interest between funders, lawyers and plaintiffs.

¹²¹ Supreme Court of Victoria, Practice Note No 9 of 2010: Conduct of Group Proceedings, [3.6].

¹²² Supreme Court of Victoria, Practice Note SC Gen 10: Conduct of Group Proceedings (Class Actions); see also *Access to Justice - Litigation Funding and Group Proceedings* (March 2018, 2018), [2.153].

¹²³ Victorian Law Reform Commission, *Access to Justice* (n 122) [2.154]-[2.156], [2.165] and Recommendation 3.

¹²⁴ Australian Government Productivity Commission (n 57) chapter 18.

¹²⁵ *ibid* 624.

¹²⁶ *ibid* 629-30.

- There is a lack of financial supervision and therefore no measures to encourage a funder to hold adequate capital relative to its financial obligations.

To address these issues, the Commission recommended that a licensing scheme be established, under which funders would be required to maintain adequate capital reserves, would be required to make proper disclosure to claimants, and to maintain systems for managing conflicts. However, it recommended that ‘the ethical conduct’ of funders should be monitored by the court, and concerns about the operation of funding in particular types of proceedings – such as class actions – should be dealt with through specific reform to those forms of proceedings.¹²⁷ It also recommended that court rules should require the existence of funding agreements to be disclosed, and enable courts to make costs orders against funders.¹²⁸ These recommendations were not effected.

In 2019, the Australian Law Reform Commission released a report on whether and how class actions and third-party litigation funding should be subject to Commonwealth regulation.¹²⁹ Its recommendations were limited to Federal Court class actions. The recommendations relevant for present purposes fell into three categories:

- First, the Federal Court with express case management powers concerning funding, including a requirement to commence as an open class, providing criteria for closing the class, and providing express power to the court to make CFOs and to resolve competing classes.¹³⁰

¹²⁷ *ibid* 633, recommendation 18.2.

¹²⁸ *ibid* 637, recommendation 18.3.

¹²⁹ ALRC, *Integrity, Fairness and Efficiency* (n 78) 5-6 (terms of reference).

¹³⁰ *ibid* 9 (recommendations 1 – 7).

This latter recommendation was particularly prescient in light of the 2019 High Court judgment in *Brewster*.

- Secondly, expanding settlement approval powers of the court – including expanding the court’s powers to assess the reasonableness of legal costs.¹³¹
- Thirdly, regulation of funders – including preventing solicitors from recovering unpaid fees from the group or a representative (essentially requiring solicitors to assume the risk of the funder running out of funds), and to include express provision in the legislation for (1) the presumption that the third party funder will provide security for costs in a form that is enforceable in Australia and (2) the power to award costs against funders who fail to comply with the overarching purpose. Separately, it is recommended that ASIC regulatory guide 248 be amended to require funders to report on their compliance with the existing conflict of interest requirements, and it is also recommended that law firm financing and portfolio financing be included in the definition of a ‘litigation funding scheme’ in Regulation 5C.11.01.¹³² This last recommendation would have the effect of extending current regulation across a broader segment of the litigation funding market. The proposed reforms would also provide that the Court has power to amend the terms of the funding agreement, that the funding agreement

¹³¹ ibid 9-10 (recommendations 8-10).

¹³² ibid 10 (recommendations 11-16).

is only enforceable with court approval, and that the agreement must include indemnity against adverse costs.

Two things are notable about these proposals. First, in many cases, the recommendations simply enshrine in legislation the solution which had already been judicially determined.

Secondly, some of the recommendations provide a level of consumer protection, reflecting concerns about the existing law and practice, especially with respect to:

- capital adequacy,
- the risk of a funder withdrawing from funding mid-way through a case,
- the ability of the court to supervise funders (particularly given that they might exercise a degree of control) and
- the possibility that the terms of the funding agreement will be disadvantageous to the claimant, having regard to the fact that class members might not understand the risk, and the difficulty in assessing whether the rate is ‘reasonable or competitive’.¹³³

These law reform proposals were relatively limited. They were directed to Federal Court class actions – not to other forms of funded proceedings, or to other courts. As at June 2020, the government had not released any response to the ALRC recommendations. However, in May 2020, the Treasurer announced that litigation funders would be required to hold an AFSL. Also in May 2020, a parliamentary enquiry was established into the ‘litigation funding and class action industry’.¹³⁴ This was

¹³³ *ibid* [6.70].

¹³⁴ Attorney-General for Australia, *Improving Justice Outcomes for Class Action Members* (2020).

spurred by reports of ‘extraordinary profits’.¹³⁵ It remains to be seen whether, and to what extent, the parliamentary enquiry gives consideration to the recommendations of the ALRC, or whether different proposals emerge.

The regulation of Australian class actions: a summary

We have seen that the regulation of class actions in Australia is in an extremely unsatisfactory state. First, judicial regulation has been productive of uncertainty and satellite litigation. Secondly, the federal structure has created obstacles to consistency of approach. Thirdly, law reform suggestions have been largely ignored, and such law reform as has been undertaken has proceeded in an unsatisfactory manner.

There are three important matters to note. Australian law reform efforts have focused on the class action funding industry. As explained in Chapter 6, this is not the entirety of the industry, and other parts of the industry have different risks and benefits, as explained in Chapter 8. Nevertheless, perceived difficulties in class actions have been used as a justification for industry-wide regulation. For example, the recent re-introduction of the requirement for funders to hold an AFSL was driven by concerns about class actions, but was applied across funders generally.

Secondly, concerns about the substantive law – such as concerns about the operation of the law concerning continuing disclosure obligations – have driven attempts to constrain litigation funding. For example, the introduction of the AFSL requirement was made using emergency powers designed to enable the government to deal with the COVID-19 pandemic, with the Treasurer being reported as reasoning that “Australian companies needed to stay in business in the current crisis rather than spend

¹³⁵ *Committee to Examine Impact of Litigation Funding on Justice Outcomes* (2020).

time ‘fending off’ class actions’.¹³⁶ The change was made despite the opposition of ASIC, and in the face of contrary recommendations made by the Australian Law Reform Commission in its most recent treatment of litigation funding.¹³⁷

Finally, there has been no attempt to start from first principles in considering the need for regulation. For example, one reason for the current Parliamentary inquiry being instigated was a concern about funders being driven by a motivation for profit, without any examination of whether and why that is undesirable (such as that undertaken in Chapter 5 of this thesis).

Judicial regulation of funding agreements entered into by insolvency practitioners

An insolvency practitioner must seek the approval of the court before entering into any contract of more than three months’ duration.¹³⁸ Accordingly, insolvency practitioners require court approval to enter into a litigation funding agreement. On such an application, the court will not seek to usurp the insolvency practitioner’s commercial judgment. Rather, the inquiry is whether entry into the funding agreement represents a bona fide exercise of the liquidator’s statutory power – a relatively low threshold, although, as the case law demonstrates, not a rubber stamp.¹³⁹

¹³⁶ David Crowe, ‘New rules for litigation funders after jump in class actions’ *Sydney Morning Herald* (22 May 2020) <<https://www.smh.com.au/politics/federal/new-rules-for-litigation-funders-after-jump-in-class-actions-20200521-p54vak.html>> .

¹³⁷ Ben Butler, ‘Frydenberg’s Changes to Shareholder Class Actions Smack of ‘Cronyism’, Lawyers Say’ *The Guardian* (25 May 2020) <<https://www.theguardian.com/australia-news/2020/may/25/frydenbergs-changes-to-shareholder-class-actions-smack-of-cronyism-lawyers-say>> ; see also The Hon Josh Frydenberg MP, *Litigation funders to be regulated under the Corporations Act* (2020).

¹³⁸ Corporations Act 2001 (Cth), s 477(2B) and s 506(1A).

¹³⁹ See generally Standing Committee of Attorneys-General, *Litigation Funding in Australia: Discussion Paper* (2006), 18.

The court will not second-guess a liquidator's commercial judgment.¹⁴⁰ Rather, the task for the court is to determine whether the liquidator has exercised the power of sale in good faith – in other words, whether the arrangement can truly be said to be a sale of property.¹⁴¹ In resolving that question, the court will consider:¹⁴²

... the nature of the cause of action, its complexity, the amount of costs likely to be incurred in the conduct of the action, the extent to which the funding entity is to contribute to the costs of the action, the extent to which the funding entity is to contribute towards the costs of the respondent in the event that the action is not successful or towards any order for security for costs by the Court before which the action is to be heard, the extent to which the liquidator has canvassed other funding options, the level of the 'premium', the risks involved in the claim, and the liquidator's consultations with the creditors of the company.

There is, however, a degree of opacity in this area of law. The court will sometimes order that a litigation funding agreement be kept confidential, even where it has been put into evidence for some other reason.¹⁴³ This is an exercise of the court's power to protect its own process:¹⁴⁴ the concern is that a defendant who knows the quantum and terms of the claimant's funding could adjust their litigation tactics accordingly, thus having an unfair advantage.¹⁴⁵ It is therefore impossible to determine precisely where Australian courts draw the line between permissible and impermissible funding arrangements.

¹⁴⁰ *Re Addstone Pty Ltd (in liq)* (1998) 83 FCR 583 (FCA), 593.

¹⁴¹ *ibid* 593-4.

¹⁴² *ibid* 594.

¹⁴³ See *Weston v Publishing and Broadcasting Limited* [2010] NSWSC 1288, [33]-[38] for a list of some such cases, and an explanation of the relevant principles.

¹⁴⁴ *ibid* [36].

¹⁴⁵ *ibid* [34].

Security for costs

The position in Australia concerning security for costs is uncertain and unsatisfactory. There is no express provision in the rules of any Australian jurisdiction for the court to order security for costs against a person other than the plaintiff.

The existence of a litigation funding agreement will be relevant to the decision whether to order security against the claimant.¹⁴⁶ In part, this has been treated as an issue of principle; as Hodgson JA explained:¹⁴⁷

... a court should be readier to order security for costs where the non-party who stands to benefit from the proceedings is not a person interested in having rights vindicated, as would be a shareholder or creditor of a plaintiff corporation, but rather is a person whose interest is solely to make a commercial profit from funding the litigation. Although litigation funding is not against public policy, the court system is primarily there to enable rights to be vindicated rather than commercial profits to be made; and in my opinion, courts should be particularly concerned that persons whose involvement in litigation is purely for commercial profit should not avoid responsibility for costs if the litigation fails.

Courts have also recognised pragmatic reasons for treating the existence of a funder as relevant to the decision whether to order security. In simplified terms, an order for security for costs is intended to protect the defendant from the risk that the claimant will not be able to satisfy a later costs order, although the court will be careful to avoid stultifying proceedings.¹⁴⁸ As to the protection of the defendant, the court will consider whether the funder has offered an undertaking to pay adverse costs, and will also consider the terms of the funding agreement, such as whether there is a power to

¹⁴⁶ Friel (n 113) 11; Adrian Zuckerman and others, *Zuckerman on Australian Civil Procedure* (LexisNexis Butterworths 2018), [10.165].

¹⁴⁷ *Green (as liquidator of Arimco Mining Pty Ltd (in liq)) v CGU Insurance Ltd* [2008] NSWCA 148; (2008) 67 ACSR 105, [51] (citations omitted).

¹⁴⁸ See generally *Zuckerman on Australian Civil Procedure* (n 146) [10.139]-[10.164] as to the general principles upon which security will be ordered.

terminate without cause.¹⁴⁹ It may also be necessary to consider the financial position of the funder, as this will affect the value of the funder's promise to pay adverse costs.¹⁵⁰

An order for security is routine in funded class actions.¹⁵¹ Even in unfunded class actions, courts may order security, and it may be necessary for group members to make a 'real, but not oppressive' contribution to security.¹⁵²

A committee of the Council of Chief Justices of Australia and New Zealand considered whether there ought to be some, minimal rules of court concerning litigation funding. One proposed rule was to permit the court to order security against the funder. However, a majority of the committee ultimately took the view that the courts ought not to make any rules concerning litigation funding without legislation.¹⁵³

In 2012, the New South Wales Law Reform Commission suggested that the court might have the power to make such an order in the exercise of its inherent jurisdiction, but the position remained untested at that time.¹⁵⁴ Nevertheless, it proposed amendments to the legislation and rules in order to align the rules concerning security for costs with those concerning costs, despite considering that such a power

¹⁴⁹ *ibid* [10.166]. See, for example, *The Australian Derivatives Exchange Ltd v Doubell* [2008] NSWSC 1174, where security was not ordered because the terms of the funding agreement were sufficient protection for the defendant, on the claimant's undertaking to inform the defendant of any termination, and to enforce the terms of the funding agreement for the defendant's benefit.

¹⁵⁰ *Friel* (n 113) 11; *Bufalo Corporation Pty Ltd (Rec & man app'td) (in liq) v Lendlease Primelife Limited & Ors (No 3)* [2010] VSC 263, [65]-[66].

¹⁵¹ *Perera v GetSwift Limited* [2018] FCA 732; (2018) 127 ACSR 1, [192].

¹⁵² *Madgwick v Kelly* [2013] FCAFC 61; (2013) 212 FCR 1, [99]; see generally Vince Morabito and Naomi Hatcher, 'Security for Costs in Unfunded Federal Class Actions: Back to the Future' (2018) 92 Australian Law Journal 105.

¹⁵³ The Hon Justice Kevin Lindgren, 'Some Current Practical Issues in Class Action Litigation' (2009) 32 University of New South Wales Law Journal 900, 903-4.

¹⁵⁴ New South Wales Law Reform Commission, *Security for Costs and Associated Costs Orders* (2012), [3.18].

would rarely be used, owing to the usual practice of funders to provide adverse costs and the available of an undertaking.¹⁵⁵

But in 2019, Lee J in *Turner v Tesa Mining (NSW)* made an order for security for costs against a funder, holding that there was inherent power to do so. The case was unusual, because it arose in the context of a class action under the Fair Work Act, which is a ‘no costs’ jurisdiction in which parties ordinarily bear their own costs.¹⁵⁶ His Honour nevertheless considered that the profit motive of the funder warranted an order for security,¹⁵⁷ explaining that:¹⁵⁸

This legislative choice [i.e. requiring parties to bear their own costs] has had the effect of safeguarding the ability of an applicant, a person often with a modest claim facing the spectre of an intimidating inequality of arms, to bring an action freed from the vexation that an adverse costs order could mean financial ruination. There is no compelling textual or contextual argument which would suggest that this protection should be somehow extended to *non-party* funders who are using these claims to their perceived commercial advantage.

As at June 2020, the judgment was under appeal. The judgement is, of course, not economically neutral. Such an order affects the access to justice of the funded party, as it increases the cost to it of funding. Indeed, in the context of ordering security against a funded claimant, it has been treated as relevant that the cost of security will ultimately be borne by the class, indirectly, as a cost of funding.¹⁵⁹

Nevertheless, it is rational that the presence of a funder would be relevant to the decision whether to order security against a claimant. In assessing the balance between protecting the defendant, and not stultifying the litigation, it is relevant that another

¹⁵⁵ *ibid* [3.27]-[3.30].

¹⁵⁶ *Turner v Tesa Mining (NSW) Pty Limited* [2019] FCA 1644, [4].

¹⁵⁷ *ibid* [41] and [71]-[72].

¹⁵⁸ *ibid* [77]; *Bywater v Appco Group Australia Pty Ltd* [2019] FCA 799, [11].

¹⁵⁹ *Perera v GetSwift Limited* [2018] FCA 732; (2018) 127 ACSR 1, [193]-[194].

party has agreed to fund the litigation – it affects the question whether the litigation will be stultified if an order is made. It is more difficult to justify the view that the funder’s profit motive is relevant.¹⁶⁰ And the current state of the law in Australia is unsatisfactory, being productive of uncertainty and satellite litigation.

England

In England, judicial regulation of litigation funding has primarily taken place in the context of costs – i.e. determining whether the funder must pay adverse costs.

The funder’s liability for adverse costs

The court has power to order that a non-party pay costs.¹⁶¹ Such an order will not be usual, but will be made, in the exercise of the court’s discretion, in circumstances where it is just to do so.¹⁶²

A ‘pure funder’ – that is, a person who has no interest in the litigation, does not seek to control the litigation and does not stand to profit from it – will not usually be ordered to pay costs.¹⁶³

Where litigation is funded by a commercial funder, the funder’s liability for adverse costs may be limited ‘to the extent of the funding provided’ – this is the *Arkin* cap, in reference to the 2005 judgment which provided its genesis.¹⁶⁴ In *Arkin* itself, the funder had paid only for the costs of expert evidence. The Court of Appeal was concerned that the prospect of adverse costs orders would deter litigation funders,

¹⁶⁰ See, eg, *Turner* (n 156) [71]-[72].

¹⁶¹ Supreme Court Act 1981 (UK), s 51.

¹⁶² *Dymocks Franchise Systems (NSW) Pty Ltd v Todd* [2004] UKPC 39; [2004] 1 WLR 2807, [25(1)].

¹⁶³ *ibid*; *Hamilton v Al-Fayed (No 2)* [2002] EWCA Civ 665; [2003] QB 1175, [6] and [49].

¹⁶⁴ *Arkin v Borchard Lines (Nos 2 and 3)* [2005] EWCA Civ 655; [2005] 1 WLR 3055, [41].

particularly if they funded only part of the proceedings such that the cost consequences were ‘disproportionate’.¹⁶⁵ Thus, a balance needed to be struck between the interests of access to justice, and the ordinary rule that costs follow the event.¹⁶⁶

The Court of Appeal also considered that the cap would have two further benefits. First, funders would be likely to impose a limit on their funding, thus making it more likely that costs would be proportionate. Secondly, funders would be more likely to scrutinise carefully the merits of funded claims.¹⁶⁷

Arkin has been a controversial judgment. Sir Rupert Jackson recommended its removal by legislation or rule amendment in his 2009 review of costs.¹⁶⁸ His Lordship observed that there was no evidence for the central premise of the judgment – namely, that exposing the funder to ‘full liability for adverse costs would stifle third party funding or inhibit access to justice’ – in fact, the Australian experience demonstrated the contrary.¹⁶⁹ Further, there was an inherent unfairness in a commercial funder sharing the spoils of victory, but not the consequences of defeat (i.e. adverse costs), which had the potential to operate unfairly to both the defendant and the funded claimant (who would, in the absence of a third party costs order, be obliged to pay adverse costs).¹⁷⁰

¹⁶⁵ *ibid* [38]-[39].

¹⁶⁶ *ibid* [38].

¹⁶⁷ *ibid* [42].

¹⁶⁸ Jackson (n 2) Chapter 11, [4.7].

¹⁶⁹ *ibid* chapter 11, [4.5].

¹⁷⁰ *ibid* chapter 11, [4.6]. Indeed, in Australia, the funder’s assumption of the risk of paying adverse costs is cited as the justification for permitting the funder to receive a generous percentage of the judgment: ALRC, *Integrity, Fairness and Efficiency* (n 78) [6.73].

The Court of Appeal has now confirmed in *Chapelgate v Money* that the *Arkin* cap is not a binding rule.¹⁷¹ The Court recognised that the risk of chilling the market by imposing adverse costs was less acute than in 2005.¹⁷² Nevertheless, the *Arkin* cap was not redundant, and would likely be applicable where the facts were ‘closely comparable’ to those in *Arkin*.¹⁷³ The Court of Appeal endorsed the trial judge’s approach to the exercise of the discretion.¹⁷⁴

In *Chapelgate* itself, it was relevant that

- The funding was for a commercial purpose.¹⁷⁵
- The conduct of the litigation had been unusual, such that an order for indemnity costs had been made,¹⁷⁶ and that although the funder had not controlled the litigation, it had provided funding after the conclusion of pleadings, discovery and exchange of witness statements, when it was able to form its own view of the merits.¹⁷⁷ In those circumstances, the funder ought not to be able to disassociate itself from¹⁷⁸ the conduct which it had enabled through its provision of funding.

¹⁷¹ *Chapelgate Credit Opportunity Master Fund Ltd v Money* [2020] EWCA Civ 246, [38], and see the earlier suggestions in *Bailey v GlaxoSmithKline UK Ltd* [2017] EWHC 3195 (QB); [2018] 4 WLR 7, [59].

¹⁷² *Chapelgate Credit Opportunity Master Fund* (n 171) [36].

¹⁷³ *ibid* [37].

¹⁷⁴ *ibid* [44].

¹⁷⁵ *Davey v Money* [2019] EWHC 997 (Ch), [91]

¹⁷⁶ *ibid* [92].

¹⁷⁷ *ibid* [93].

¹⁷⁸ *ibid* [94].

- The funder was aware that the claimant was impecunious, and that the defendants' costs were likely to be far greater than the funder's investment.¹⁷⁹
- When the claimant had been unable to secure ATE insurance, the funder had reduced its commitment, whilst retaining its profit share.¹⁸⁰
- The funder's profit in the event of success was to take priority over any return to the claimant.¹⁸¹ Indeed, the structure of the funding agreement (and the likelihood of the claimant receiving any compensation) was such that the funder had the primary interest in the litigation.¹⁸²
- There was no evidence that the disapplication of the *Arkin* cap would have a chilling effect on the industry,¹⁸³ and this was *a fortiori* in light of the Court of Appeal in *Excalibur* having encouraged funders to monitor costs.¹⁸⁴

Chapelgate was a relatively extreme case. It must therefore be said that although it is now clear that the *Arkin* cap is not a rule to be applied mechanically and inflexibly, it is not clear where the dividing line will be. For example, is it the case that the *Arkin* cap ought only to be applied to cases of partial funding? Is a departure from the *Arkin* cap justified only where the funder has the primary interest in the litigation?

¹⁷⁹ *ibid* [95].

¹⁸⁰ *ibid* [96].

¹⁸¹ *ibid* [99].

¹⁸² *ibid* [101]-[105].

¹⁸³ *ibid* [106]-[108].

¹⁸⁴ *ibid* [109]-[110].

The *Arkin* cap continues to be applied, but there must be some uncertainty about its bounds.¹⁸⁵

A litigation funder may be ordered to pay costs on an indemnity basis, if an order to that effect is made through the application of the ordinary rules concerning costs.¹⁸⁶ Where the *Arkin* cap applies, amounts provided by the funder as security for costs will count towards the quantum of the cap.¹⁸⁷

The rules in all but one of the Australian jurisdictions enable a defendant to seek an order for third party costs against a litigation funder.¹⁸⁸

Funder's liability for security for costs

The English CPR contain express provision for security for costs to be ordered against a funder.¹⁸⁹ The power is limited to persons against whom an order for costs may be made, and so pure funders would usually be excluded from the operation of the rule. In *In re RBS Rights Issue Litigation*¹⁹⁰ Hildyard J identified that the factors relevant to whether such an order would be made were:

(1) whether it is sufficiently clear that the non-party is to be treated as having in effect become in all but name a real party motivated to participate by its commercial interest in the litigation; (2) whether there is a real risk of non-payment such that security against the contingent liability should be granted; (3) whether there is a sufficient link between the funding and the costs for which recovery is sought to make it just for an order to be made; (4) whether a risk of liability for costs has sufficiently been brought home to the non-party, either by express

¹⁸⁵ *Burnden Holdings (UK) Ltd v Fielding* [2019] EWHC 2995 (Ch).

¹⁸⁶ *Excalibur Ventures LLC v Texas Keystone Inc* [2014] EWHC 3436 (Comm); [2014] 6 Costs LO 975.

¹⁸⁷ *Excalibur* (n 6) [32]-[41].

¹⁸⁸ Lisa Bench Nieuwveld and Victoria Shannon Sahani, *Third-Party Funding in International Arbitration* (2nd edn, Kluwer Law International 2017), 87; 'The Rise and Regulation of Litigation Funding in Australia' (2011) 38 Northern Kentucky Law Review 625, 647 The exception is the Australian Capital Territory, which is a very small jurisdiction.

¹⁸⁹ CPR 25.14(2)(b).

¹⁹⁰ *In re RBS Rights Issue Litigation* [2017] EWHC 1217 (Ch); [2017] 1 WLR 4635, [19]

warning, or by reference to what a person in its position should be taken to appreciate as to the inherent risks; (5) whether there are factors, including for example, delay in the making of an application for security or likely adverse effects such as to tip the overall balance against making an order.

In assessing the first criterion, the motivation of the funder (i.e. commercial or altruistic) is important.¹⁹¹ His Lordship held that if the funder was commercial, then ‘the policy is likely to be to visit the consequences and costs of a commercial venture on the adventurer’.¹⁹² In a subsequent judgment, it was held that it was also relevant to consider the possibility that the *Arkin* cap would be applied at the end of the proceedings.¹⁹³

Problems with judicial regulation

The difficulty with court-imposed regulation is six-fold. First, judgments are, by their nature, retrospective and piecemeal. They address legal problems in the context of a unique fact situation.¹⁹⁴ The precedential force of a judgment may be limited, or may be uncertain. For example, as explained above in the context of considering *Chapelgate*, it may be unclear where the line will be drawn in future cases. In the federal structure of Australia, there is the added difficulty that intermediate appellate courts are not strictly bound by the ratio of equivalent courts in other jurisdictions,¹⁹⁵ and the legislation creating class actions may be different in each state, so judgments delivered in one jurisdiction may have a limited or unclear precedential value in others.

¹⁹¹ *ibid* [20].

¹⁹² *ibid* [22].

¹⁹³ *Bailey v GlaxoSmithKline UK Ltd* [2017] EWHC 3195 (QB); [2018] 4 WLR 7, [58]-[61].

¹⁹⁴ Marc Galanter, ‘Why the “Haves” Come out Ahead: Speculations on the Limits of Legal Change’ (1974) 9 *Law and Society* 95, 137, 138.

¹⁹⁵ *Australian Securities Commission v Marlborough Gold Mines Ltd* (1993) 177 CLR 485.

Secondly, there is also inherent uncertainty owing to the possibility of a judgment being appealed. The path of CFOs in Australia provides a good example of this – for several years, courts built a body of jurisprudence in this area, only for the High Court to determine that the court had no power to make such an order.

Thirdly, relying on incremental judicial decisions necessarily requires satellite litigation. This is wasteful of the time and money of the parties, and the court. It also means that developments in the law are adventitious: they will only occur if a party pursues a particular point. In some of the cases which have tested the boundaries of the doctrine of champerty, for example, the assertion that an agreement is unenforceable as being champertous has not been made by the funded claimant (who is party to the agreement), but rather by the defendant to the funded action. In the context of Australian CFOs, the law changed in *Brewster* only because a party was prepared to pursue the point to the ultimate appellate court. It is unsatisfactory that developments in the law require the impetus and initiative of individual litigants. Given the cost of pursuing satellite litigation, it seems likely that well-resourced litigants would seek developments in the law more frequently than the impecunious, and this has the potential to distort the law.¹⁹⁶

Fourthly, there is a question about the institutional competence of a court to regulate. A court is not a legislature; it cannot create general prospective rules beyond what is necessary to resolve the case before it. Further, a court cannot seek expert advice, conduct research or carry out public consultations in order to devise regulatory solutions. In *Arkin*, for example, the Court of Appeal relied (in part) on the empirical assumption that exposing the funder to adverse costs would chill the market – an

¹⁹⁶

The point was discussed in Chapter 3.

assumption which many queried in light of the Australian experience to the contrary. The Australian experience concerning costs in class actions is a particularly good example of this problem: courts have devised a variety of solutions to the problem of how to fairly allocate costs, but as they have done so, market practice has shifted in response, necessitating further rule-development.

Fifthly, a court is also limited in its ability to craft solutions. It cannot, for example, ‘devis[e] new regulatory or administrative machinery’.¹⁹⁷ This means that the court’s range of solutions is limited. But it also means that there are some problems which the court cannot even attempt to address. For example, in the litigation funding context, a court could not create rules concerning the capital adequacy of funders, nor could it mandate the provision of information in claimants in order to address problems of information asymmetry – both of these problems are, essentially, beyond the remedial powers of the court.

Finally, courts are not well-placed to create changes in rules. Rules are more likely to be sought by repeat players and by one-shotters, owing to the fact that rule changes are more likely to affect them, and are expensive to obtain.¹⁹⁸ Indeed, we can see that in the Australian class action context, rule changes have been driven by funders. One might expect, therefore, a disproportionate number of rules concerning the issues which are primary the concern of funders, rather than the issues which primarily concern the funded claimant.

¹⁹⁷ Galanter (n 194) 137.

¹⁹⁸ *ibid* 136.

Laws of general application, which might apply to litigation funding

In some Australian jurisdictions, certain duties to the court are imposed on persons who provide financial assistance and assert some control or influence over the proceedings,¹⁹⁹ which would apply to funders (amongst others). In Victoria, the funder is subject to the overarching obligations, which include obligations to ‘further the administration of justice’ and to ‘act honestly’, amongst other things.²⁰⁰ In Western Australia, a party must notify the Registrar and the other parties of the existence and identity of any interested non-party; the non-party is subject to an obligation to cooperate, not to mislead or deceive, and to further the case management objectives prescribed by the Rules.²⁰¹ In New South Wales, the duty is far more limited: a funder must not cause a party or their lawyer to breach their duty to further the overriding purpose of ‘facilitat[ing] the just, quick and cheap resolution of the real issue.’²⁰²

Litigation funding agreements will be subject to general principles of law which apply to all contracts. At common law, the doctrine of unconscionability may be used to set aside contracts where one of the transacting parties has taken unconscionable advantage of some special disability of the other party; for example, illiteracy, inability to speak English, emotional dependence, or mental incapacity.²⁰³ It does not, however, affect the position where there is a mere inequality of bargaining power.²⁰⁴

¹⁹⁹ Duffy (n 53) footnote 167.

²⁰⁰ Civil Procedure Act 2010 (Vic), ss 10-12 and 16-27, especially 10(d).

²⁰¹ Rules of the Supreme Court 1971 (WA), Order 9A.

²⁰² Civil Procedure Act 2005 (NSW), s 56.

²⁰³ *Commonwealth Bank v Amadio* (1983) 151 CLR 447; see generally Jeannie Paterson, Andrew Robertson and Arlen Duke, *Principles of Contract Law* (4th edn, Thomson Reuters 2012), Chapter 36.

²⁰⁴ *ACCC v Berbatis Holdings P/L* [2003] HCA 18; (2003) 214 CLR 51.

The equitable doctrine of mistake as to terms may also apply if the claimant is seriously mistaken about an important term in the funding agreement, to the knowledge of the funder, and the funder fails to correct the misapprehension.²⁰⁵ Misrepresentation of fact which induces entry into a funding agreement can be a ground of rescission and/or for seeking damages.²⁰⁶

Commercial sanctions for unscrupulous behaviour?

There is a body of empirical research which demonstrates the utility of trust and reputation – rather than legal sanction – as a means of enforcing norms of commercial behaviour, particularly in self-contained industries where participants are known to each other.²⁰⁷ In a variety of industries, it has been observed that self-generated norms, sometimes enforced via private systems of arbitration, and underpinned by sanctions in the form of loss of reputation – leading to adverse business and even social consequences – may replace the use of contract law and public courts as a means of enforcing standards.²⁰⁸

²⁰⁵ *Taylor v Johnson* (1983) 151 CLR 422, 432; Jeannie Paterson, Andrew Robertson and Arlen Duke, *Principles of Contract Law* (4th edn, Thomson Reuters 2012), [31.123] and generally Chapter 31.

²⁰⁶ Paterson (n 205) Chapter 31.

²⁰⁷ Referred to and summarised by John Gava, 'How Should Judges Decide Commercial Contract Cases?' (2013) 30 *Journal of Contract Law* 133, 134-6, 137. Some of this research has focused on the use of 'private ordering', through self-regulation and the use of reputation – rather than the law of contract, and resort to public courts – to enforce obligations which arise in particular transactions. See Barak D Richman, 'Firms, Courts, and Reputation Mechanisms: Towards a Positive Theory of Private Ordering' (2004) 104 *Columbia Law Review* 2328, 2337-50 as to the circumstances in which private ordering has been observed in empirical research, the reasons why it is preferable to the use of public courts in each.

²⁰⁸ Particularly famous examples include Bernstein's studies of the New York Diamond Dealers' Club, and the cotton industry in the southern United States. In each of these industries, a private system of arbitration had developed, but norms were often enforced through reputational damage, industry gossip, and the resulting threat of adverse consequences to the wrongdoer's business, and indeed these sanctions also formed the basis for the operation of the arbitration system: see generally Lisa Bernstein, 'Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry' (1992) 21 *Journal of Legal Studies* 115; Lisa Bernstein, 'Private Commercial Law in the Cotton Industry: Creating Cooperation through Rules, Norms, and Institutions' (2001) 99 *Michigan Law Review* 1724.

More broadly, and relevantly for present purposes, it has been hypothesized that ‘members of a tight-knit group develop and maintain norms whose content serves to maximize the aggregate welfare that members obtain in their workaday affairs with one another’.²⁰⁹ The suggestion is that, where conditions are right, a tight-knit group – which could be a professional community – can implement and enforce ‘mutually wealth-enhancing norms of conduct’ through ‘self-enforced social sanctions’.²¹⁰

For example, it has been suggested that one reason for Silicon Valley’s ascendancy in the technology industry is that engineers in the region developed a social norm of collaborating and sharing information with competitors, and eschewing reliance on intellectual property rights, a culture which was fostered by (amongst other things), the geographical proximity of their employers, close social connections, and high mobility between employers.²¹¹ These norms were enforced through professional and social sanctions: companies which sought to enforce their intellectual property rights were excluded from collaboration, and employees of such companies were not included in professional networks. Further, engineers were reluctant to work for such firms.²¹²

Waye’s small study of the Australian class action funding industry contains glimpses of practices and attitudes which echo this body of work. Her interviews with funders and solicitors indicates that there are substantial commercial pressures on both to be ‘model citizens’. First, as has been explained earlier in this chapter, the regulatory

²⁰⁹ Robert C Ellickson, *Order Without Law: How Neighbours Settle Disputes* (Harvard University Press 1991), 167.

²¹⁰ Richman (n 207) 2357-62.

²¹¹ See AnnaLee Saxenian, *Regional Advantage: Culture and Competition in Silicon Valley and Route 128* (Harvard University Press 1996), especially Chapter 2.

²¹² Richman (n 207) 2359.

regime in Australia has been unsettled for many years, with repeated calls for further regulation. Funders have been active in lobbying and making submissions to law reform commissions. Secondly – and in part owing to various lacunae in regulation – funders have been active in litigating for the purpose of driving the development of the law in a manner favourable to them; these efforts have been successful insofar as Australian courts have delivered judgments providing for practices such as closed classes and common fund orders.²¹³ Funders and law firms recognise that their success on both fronts is aided by establishing a good reputation.²¹⁴

Specifically, one aspect of maintaining a good reputation that funders and firms have recognised – particularly in light of the requirement for court approval of settlements in class actions – was the need to avoid any suggestion that the funder and solicitor had colluded to their mutual advantage, and contrary to the interests of class members.²¹⁵ The importance of maintaining a good reputation meant also that solicitors were concerned only to engage with reputable funders.²¹⁶

On the other hand, funders were also concerned to avoid the possibility of a solicitor becoming complacent, and so were eager to avoid relying too heavily on particular firms of solicitors. Thus, there were competitive pressures in the market for class action solicitors, despite its small size.²¹⁷

²¹³ Vicki Waye, 'The Initiation and Operations Phase of the Litigation Funder - Class Action Law Firm Relationship: an Australian Perspective' (2018) 60 *International Journal of Law and Management* 595, 605-6.

²¹⁴ *ibid* 613-14.

²¹⁵ *ibid* 614.

²¹⁶ *ibid* 604.

²¹⁷ *ibid*.

Waye's work suggests that the market has, in effect, created norms of scrupulous behaviour which are enforced through reputational sanctions. For example, Waye reports that:²¹⁸

... given Australia's cultural opprobrium for claim commodification, it is important from the perspective of each prospective partner in the funder-class law firm alliance that each presents itself as a champion for access to justice rather than a mere "trafficker" in litigation. One funder commented that "any disreputable behaviour is likely to be quickly and widely known and business will suffer. The class action community in Australia is very small and intertwined and (so) bad or unreasonable behaviour will be detrimental to the funder's business"....

Consistently with the use of reputation and ongoing relationships as a means of enforcing standards – rather than contractual terms – Waye also reported that contracts between funders and solicitors were brief; her research reported that:²¹⁹

All parties commented that they relied upon discriminating partner selection and ongoing monitoring and communication rather than complex contractual provisions to safeguard against performance, relational and regulatory risk.... careful selection of a reliable and competent funder or class law firm appears to have obviated the need for detailed and complex contractual provisioning. Rather than acting as an instrument of governance, the contract between the law firm and funder thus constitutes a symbol of commitment to the relationship and a means to implement "contingency adaptability" arising from unforeseen environmental factors or unanticipated inter-party conflict.... Even where the contract was reasonably lengthy, the parties indicated that they did not spend a great deal of time negotiating its terms, as they all believed that the primary agreement of concern was the agreement between the funder and class members. [citations omitted]

Thus, it appears that in the Australian class action context at least, the nature of the market is such that there is self-enforcement of certain norms of conduct. This includes behaving in a manner which is, and is seen to be, ethical. The perceived

²¹⁸ ibid 603.

²¹⁹ ibid 607.

advantages of this include being able to persuade the court to make incremental developments in the law which are favourable to funders (as has, in fact, happened).

One might take the view that in light of the commercial pressure to conform to ethical standards, regulation might be less necessary than would otherwise be the case. However, the litigation funding industry is growing rapidly, with an increase in new entrants. Further, the barriers to entry in the class action context – the ability to deal with the logistics of coordinating a large class, and completing a book-build – are not present in other sectors of the litigation funding market. It must therefore be doubted whether (1) the self-enforcement of norms would exist in other sectors of the funding market, or in jurisdictions where regulation has not been as contentious and/or (2) the current informal self-regulation will continue in the class action sector, as the size of the market increases, as the need for further favourable court judgments subsides, and if the scrutiny of regulatory attention subsides.

In any event, Waye's study focused attention on the views of funders and solicitors towards each other. One of the concerns about the industry is the possibility that funders and solicitors will collude (to the disadvantage of the claimant(s)); it is unknown whether the market dynamics which Waye has reported would operate to the benefit of claimants, particularly given the fact that many claimants in class actions will be 'one-shotters'.

The more likely view is that the current commercial pressures, which are encouraging scrupulous behaviour by funders and solicitors, are unlikely to continue. Regulation will, therefore, become increasingly necessary as the market expands and matures.

Conclusion

The current state of regulation of litigation funding is unsatisfactory. First, the principal sources of regulation are voluntary codes and judicial regulation. The former is limited in its application; the latter suffers from the inherent limitations of judicial regulation (many of which can, in fact, be observed in the jurisprudence on litigation funding, as explained above). Regulation has also been piecemeal, arising adventitiously, rather than because of careful consideration of the issues and possible responses. Further, there is no nuance as to the different markets – for example, in Australia, regulatory efforts have focused on the class action market, but, as was explained in Chapter 6, this market operates differently to other parts of the funding market.

It is common to hear calls for the litigation funding industry to be regulated, or for market participants to resist the suggestion that regulation is needed. However, both arguments rest on the flawed premise that litigation funding is not regulated. The reality is that the litigation funding industry is regulated in a piecemeal manner, partly by voluntary codes, partly by the uncertain application of existing law to the novel position of a funder (such as, in England, the application of principles concerning third party liability for costs, and in Australia, the application of legislation concerning financial regulation to funders), and partly by judicial regulation (as in Australian class actions).

The existing debate about regulation has also suffered from two limitations. First, the question of regulation has not started from first principles; there has been no evaluation of the benefits of control, for example, or whether and how the profit motive of the funder is objectionable in the context of the modern civil justice system. Secondly, Australian law reform efforts have focused on the class action funding

industry, and perceived difficulties in that area have driven industry-wide regulation, with no consideration for the diversity of the market.

In the next chapter, some broad suggestions for how regulation might be reformed and progressed are considered, using the framework of the market failures identified in the last chapter.

CHAPTER 10: REGULATING THE RELATIONSHIP BETWEEN FUNDER AND CLAIMANT

Introduction

I explained in the last chapter that existing regulation of litigation funding is piecemeal and unsatisfactory. In this chapter, I return to some of the risks of the market, identified in Chapter 8, and make some general suggestions as to regulatory options.

The six principal risks are:

- that the claimant will enter a funding agreement on disadvantageous terms;
- that the funder will exert a level of control beyond that anticipated by the claimant;
- the possibility that, once the litigation is in progress, the funder becomes *unwilling* to discharge its future funding obligations ('the termination risk');
- the possibility that, once the litigation is in progress, the funder will run out of capital and will thus be *unable* to discharge its future funding obligations ('the capital adequacy risk');
- the possibility that the funder will not assume liability for adverse costs orders; and/or
- the possibility that disputes will arise between funder and claimant concerning the conduct of the litigation – such as disputes concerning litigation strategy, or whether to accept an offer of settlement.

In particular, I draw on the analysis of market failures in Chapter 7 to think about the cause of each of these risks, and how they might be regulated.

At the end of the chapter, I will address briefly a further difficulty in regulation: difficulties which have been encountered in fitting litigation funding into existing rules of practice, such as rules about adverse costs.

Entry into the litigation funding agreement – disadvantageous terms

The first risk that arises is that a claimant will contract on disadvantageous terms.¹ This risk arises because of information asymmetry and/or because of disparities in bargaining power.

A concern for vulnerable litigants ought not to be overstated, though. Without funding, a claimant may be forced to abandon claims altogether, meaning their loss is entirely uncompensated, or to settle with the defendant. Defendants are not regulated qua their role as defendant, nor do they have any ethical obligations to the claimant, nor are there any general laws restricting the value of settlements.² Their economic interest lies in seeing the claimant receive nothing. A funder, on the other hand, provides funds on a non-recourse basis, and therefore has an interest in seeing the claimant achieve some measure of success (at least enough to cover the funder's own costs and provide an economic return to the funder). Are we to believe that a vulnerable claimant would

¹ See Rachael Mulheron and Peter Cashman, 'Third Party Funding: A Changing Landscape' (2008) 27 *Civil Justice Quarterly* 312, 333-40, where the authors 'develop[] a list of criteria which... could form the basis for up-front "soft regulation"'. Several of the risks they identify are in the nature of disadvantageous terms – see especially 'Has the funder "monopolised" the litigation?', 'Is there a conflict of interest between the funder and the client?', 'Was the client fully informed by the funder about the effects of the funding agreement?' and 'Has the funder negotiated an "inordinately high" fee?'.

² An obvious exception is Australian class actions, where the court must approve settlement, and the parties must demonstrate that the proposed settlement is fair and reasonable: *Federal Court Act 1976 (Cth)*, s 33V; *Federal Court of Australia, Class Actions Practice Note (GPN-CA)*, [14]-[16].

be more likely to be exploited by a rogue funder than by a defendant, who ex hypothesi has caused the loss which has led to the claimant's predicament? A consideration of the risks of exploitation of vulnerable claimants by *funders* must also weigh the risks of exploitation by *defendants* in the absence of funding.

Three issues require consideration here: the adequacy of the information provided to the claimant concerning the terms of the funding agreement, terms setting the funder's percentage return, and terms concerning funder control of the litigation.

Adequacy of disclosure of terms

The risk that a claimant may not be properly informed about all material aspects of a funding agreement has long been recognised in theory,³ and there is some suggestion that it might occur in practice, too.

The issue is particularly acute in class actions, where claimants might have little contact with the solicitors (if any). It was illustrated by allegations made recently in the context of an Australian class action against various labour hire companies for their alleged underpayment of casual workers.⁴ The Australian Industry Group, which represents the interests of employers, wrote to the ACCC asserting that class members had not been aware that the funder was entitled to a 250% return on its expenditure before the class would receive any return (or 350% in the event of an appeal), and that this constituted misleading and deceptive conduct. The agreement was unusual for an Australian class action, because it did not impose a percentage, but instead calculated the funder's return as a multiple of expenditure. The claimants were invited to agree to

³ John Walker, 'Policy and Regulatory Issues in Litigation Funding Revisited' (2014) 55 *Canadian Business Law Journal* 85, 94.

⁴ 'Class Action Funding Deal over Casuals Referred to ACCC' *Australian Financial Review* (11 October 2018) <<https://www.afr.com/news/policy/industrial-relations/class-action-funding-deal-over-casuals-referred-to-acc-20181011-h16iy7>> .

the funding agreement via a link on a dedicated website, but the funding agreement only specified the funder's return in the schedules. The solicitor and funder have denied any wrongdoing, with the solicitor stating that it provided advice beyond the content of the website. Nevertheless, one can readily appreciate the difficulties in ensuring that claimants are appropriately apprised of the contents of funding agreements in these sorts of circumstances.

There may be a simple solution to this problem: to mandate the provision of information in a standard form.⁵ The standard form might identify the funder's percentage or other return (perhaps with sample calculations as to the likely return in various outcomes), the funder's assessment as to the probability of success (which would justify the rate) and the funder's estimate of the likely time to settlement or judgment.

Percentage return

Particularly in the context of class actions, concern has been expressed about the potential for claimants to receive less than 50% of proceeds after lawyers' fees and the funder's return.⁶

⁵ Contrast Poonam Puri, 'Profitable Justice: Aligning Third-Party Financing of Litigation with the Normative Functions of the Canadian Judicial System' (2014) 55 *Canadian Business Law Journal* 34, 51, who recommends the 'disclosure of the financier's model for assessing the litigation risk, probability of a favourable judgment, time-horizons for a potential settlement or judgment, the risk-adjusted profit margins for the loan, and the firm's historic accuracy in assessing the probability of a favourable judgment.' Whilst all of these matters are relevant to the question whether the funder's return is proportionate, they are not necessarily all matters which the claimant would be able to assess – for example, the risk-adjusted profit margin is meaningless in the absence of comparators from other funders.

⁶ See, eg, David Marin-Guzman, 'A Real Worry': Judge Slams Litigation Funding Fees' *Australian Financial Review* (30 May 2019) <<https://www.afr.com/leadership/workplace/a-real-worry-judge-slams-litigation-funding-fees-20190529-p51sao>> .

It is unknown what a typical percentage return is. Such data as is available is not always consistent.⁷ There is more data concerning rates in Australia, where it has been reported (inter alia):

- in 2006, the Standing Committee of Attorneys-General reported a 1/3 to 2/3 return to the funder was usual, but it could be up to 75% in insolvency cases;⁸
- on the other hand, the Law Council of Australia reported typical figures of 15-40%;⁹
- in 2012, Barker reported that typical funder returns were 20-45%;¹⁰
- in a 2018 submission to the ALRC, Maurice Blackburn (a class action claimant firm) reported that across the 16 funded class actions in which it had acted since 2016, the funder had received profits of \$283 million out of \$1,108 million in total settlements – an average of 26% - and that 60% was returned to the claimants;¹¹
- in its 2018 financial results, IMF reported that its historical average share had been 23%, and that 62% had been returned to claimants. The historical total included cases lost, and it seems likely (although it was not expressed) that this would apply to the Maurice Blackburn figures too.

⁷ See the summary of various estimates in George R Barker, 'Third-Party Litigation Funding in Australia and Europe' (2012) 8 *Journal of Law, Economics and Policy* 451, 485, and Australian Government Productivity Commission, *Access to Justice Arrangements (Productivity Commission Inquiry Report No 72)* (2014), 622. See also *Earglow Pty Ltd v Newcrest Mining Limited* [2016] FCA 1433, [166]-[178] as to the range of percentages.

⁸ Standing Committee of Attorneys-General, *Litigation Funding in Australia: Discussion Paper* (2006), 4.

⁹ Barker (n 7) 485.

¹⁰ Ibid.

¹¹ Maurice Blackburn, *Submission to the Australian Law Reform Commission - Inquiry into Class Action Proceedings and Third-Party Litigation Funders* (2018), [5.7].

The lack of information about usual percentages is a hindrance both to claimants, who are less able to compare the market, and to the court. In the Australian class action context, it has been explained that it is difficult for the court to assess whether a funding commission is fair and reasonable in the absence of comparators.¹² Further, although the court must approve the settlement – including the costs of litigation funding¹³ – it is an imperfect solution, because the court does not necessarily have all the information necessary to make an assessment, and also because the court’s assessment is made after the event, when there is a risk both of an element of hindsight, and also of an ‘anchoring’ effect in which the funder’s bargained-for percentage is the starting point for any assessment.

An important factor in the cost of litigation finance which is *not* emphasised by funders is the extent of competition in the market. There is some evidence to suggest that the funder’s percentage has decreased as competition has increased.¹⁴

The risk of a funder seeking a large percentage return is greater in class actions. There are two reasons for this. First, an individual claimant is less able to bargain for a lower percentage return. Indeed, claimants – particularly small claimants – will usually be offered funding on standard terms. Secondly, it was explained in Chapter 6 that funders have a rational commercial reason to ensure that funding agreements leave a good share of any proceeds to the claimant, to ensure that the claimant remains motivated to pursue its claim. This consideration is reduced, if not entirely absent, in class actions, where individual claimants may have little if any involvement in the prosecution of their claim.

¹² *Earglow* (n 7) [176].

¹³ Federal Court of Australia, Class Actions Practice Note (GPN-CA), [16.4].

¹⁴ *Earglow* (n 7) [174]; see also *Marin-Guzman* (n 6).

A funder might seek a percentage return which is higher than justified, having regard to the risk of the litigation. Funders have obligations to their shareholders to maximise profits. But, as discussed in Chapter 6, different funders are likely to have different costs of capital, and appetites for risk, and reasonable minds might differ about the merits of a claim. For these reasons, the percentage sought by different funders may vary. Brokers report that the price variance between funders may be very large.¹⁵

Regulatory options

The risk of the funder seeking an excessive percentage is largely a problem of information asymmetry, although unequal bargaining power may also play a role. Information asymmetries are usually best rectified through regulation which aims to increase information.¹⁶ The use of brokers is a partial solution, but it also increases the costs, and might not be viable in some contexts (such as class actions, where the funder instigates the claim).

There are a variety of ways in which this information asymmetry could be reduced. First, part of the present difficulty is that the due diligence process makes comparison between funders more difficult. Restrictions on the length of time permitted for due diligence, or restricting the ability of funders to impose exclusivity arrangements, would alleviate this problem. However, imposing restrictions on the due diligence process might increase the funder's rate, because it would have the tendency of making investment riskier.

¹⁵ TheJudge, 'Case Example: How Much do Litigation Funders Prices Differ for Large Cases?' (2014) <<https://www.thejudgeglobal.com/case-example-how-much-do-litigation-funders-prices-differ-for-large-cases/>> accessed 3 August 2020.

¹⁶ Circular A-4, September 17, 2003: Regulatory Analysis, 9. See also *Australian Government Guide to Regulatory Impact Analysis* (2020), 25. But compare Cass Sunstein, *After the Rights Revolution: Reconceiving the Regulatory State* (Harvard University Press 1990), 52-3.

Greater transparency of funding agreements might also assist. There are risks associated with permitting the disclosure of actual funding agreements, particularly those which are presently on foot.¹⁷ However, requiring funders to make publicly available ‘standard’ agreements, or examples of agreements on concluded matters, would provide information about the sorts of matters ordinarily dealt with in funding agreements, and permit comparison between funders – as would the creation of an ‘indicative’ contract by a regulator. Of course, there is likely to be a wide variance in the percentage charged. But standard or indicative terms of business may nevertheless be useful in the bargaining process: for example, if a funder wished to depart from the usual terms of business, or impose a higher than average percentage, it would be incumbent on the funder to explain to the claimant the reason.

It has been suggested that percentage returns could be capped.¹⁸ However, this would create several difficulties. First, the funder’s percentage may be affected by external matters such as its own cost of capital; it would be difficult to specify a percentage range which would capture those external factors. Secondly, it might effectively prevent funders taking on litigation where the law is unsettled, by preventing them from charging a high percentage commensurate with a high risk. Thirdly, a simple cap on the percentage would not prevent ‘overcharging’ by the funder. For example, if the cap were, say, 40%, a funder would not be restrained from charging 40%, even if the risk and merits of the case justified a more modest percentage of, say, 20%.

It must be acknowledged that there is a tension here. On one hand, erecting hurdles to entry to the litigation funding market – such as capital adequacy

¹⁷ Specifically, the risk arising from a defendant knowing the quantum and terms of the claimant’s funding: *Weston v Publishing and Broadcasting Limited* [2010] NSWSC 1288, [34].

¹⁸ Puri (n 5) 50.

requirements, or a licensing regime – may offer a measure of consumer protection. But, on the other hand, such measures might also create barriers to new players hoping to enter the market. This would have a tendency to decrease competition (and therefore perhaps increase prices).

Control

The question of control raises several issues. First, there is the question of what level of control ought to be permissible. The present approach of the courts and industry self-regulatory codes differs between jurisdictions.

Secondly, there is the question whether terms about control of the litigation, including terms concerning what happens in the event of a settlement offer, might be drafted in such a way as to give the funder a level of control which the claimant is unwilling to cede, or does not anticipate.

Thirdly, there is a possibility that expectation and practice will not align. As will be seen, it seems that different industry participants expect different levels of involvement, and use terms like ‘monitoring’ and ‘supervising’ to mean quite different things.

Who controls the litigation?

Law

As explained in Chapter 7, the extent of funder control which is contemplated by industry self-regulatory guides varies considerably between Australia and England. A notable difference between the ALF Code and the ALFA Guidelines is that only the former prohibits funders from ‘*seek[ing] to influence [the lawyers]... to cede control*

or conduct of the dispute to the Funder'.¹⁹ This reflects a divergence in the case law. Nevertheless, the ALF Code indicates that the funding agreement must state whether and how the funder may provide input into settlement.²⁰

In England, control by a funder of litigation is a matter which could lead to the funding agreement being categorised as unenforceable on the ground of champerty.²¹ There is a clear perception that if the funder were to seek control under the terms of the funding agreement, or were to provide instructions over the will of the client, that could lead to the funding agreement being void as contrary to public policy.²² Further, a funder who controls litigation to an impermissible extent will lose the benefit of the *Arkin* cap (that is, the funder's liability for adverse costs would be unlimited, rather than being capped at the amount of funding they have provided), thus providing a further disincentive to the funder to seek control.²³ However, the position is perhaps more nuanced following the judgments in the *Excalibur* proceedings. In that case, funders were ordered to pay indemnity costs in circumstances where the funded litigation was entirely unmeritorious and the judge had made a series of damning observations about the manner in which it had been conducted. In a statement which

¹⁹ Association of Litigation Funders, *Code of Conduct for Litigation Funders* (2018), [9.2], [9.3].

²⁰ *ibid* [11.1].

²¹ *Papera Traders Co Ltd v Hyundai (Merchant) Marine Co Ltd (The 'Eurasian Dream') (No 2)* [2002] EWHC 2130 (Comm); [2002] 2 Lloyd's Law Report 692, [43(4)] and [45]; *London & Regional (St George's Court) Ltd v Ministry of Defence* [2008] EWHC 526, [103(d)]; Nick Rowles-Davies, *Third Party Litigation Funding* (Jeremy Cousins QC ed, Oxford University Press 2014), [2.126].

²² Lord Justice Rupert Jackson, *Review of Civil Litigation Costs: Preliminary Report* (2009), Chapter 15, [3.2]; Rowles-Davies, (n 21) [1.33].

²³ *Arkin v Borchard Lines (Nos 2 and 3)* [2005] EWCA Civ 655; [2005] 1 WLR 3055, [40]-[41]; Rowles-Davies, (n 21) [2.127].

was expressly approved on appeal,²⁴ Christopher Clarke LJ rejected the suggestion that his order would have a chilling effect on the litigation funding industry, stating²⁵

If [the award of indemnity costs] serves to cause funders and their advisors to take rigorous steps short of champerty, i.e. behaviour likely to interfere with the due administration of justice, – particularly in the form of rigorous analysis of law, facts and witnesses, consideration of proportionality and review at appropriate intervals – to reduce the occurrence of the sort of circumstances that caused me to order indemnity costs in this case, that is an advantage and in the public interest.

The Court of Appeal regarded as ‘unrealistic’ the suggestion that this could effectively require the funder to exert greater control, but agreed that funders may be in a position to prevent the sort of conduct which had led to the order for indemnity costs, explaining further that:²⁶

... What the judge characterised as “rigorous analysis of law, facts and witnesses, consideration of proportionality and review at appropriate intervals” is what is to be expected of a responsible funder – as the ALF to some extent acknowledges and as did some of the funders in this case in their evidence presented to the judge – and cannot of itself be champertous. I agree... that, rather than interfering with the due administration of justice, if anything such activities promote the due administration of justice. For the avoidance of doubt I should mention that on-going review of the progress of litigation through the medium of lawyers independent of those conducting the litigation, a fortiori those conducting it on a conditional fee agreement, seems to me not just prudent but often essential in order to reduce the risk of orders for indemnity costs being made against the unsuccessful funded party. When conducted responsibly, as by the members of the ALF I am sure it would be, there is no danger of such review being characterised as champertous.

²⁴ *Excalibur Ventures LLC v Texas Keystone Inc* [2016] EWCA Civ 1144; [2016] 6 Costs LO 999, [27], and see also [31] (Tomlinson LJ; Gloster and David Richards LJ agreeing).

²⁵ *Excalibur Ventures LLC v Texas Keystone Inc* [2014] EWHC 3436 (Comm); [2014] 6 Costs LO 975, [129].

²⁶ *Excalibur Ventures* (n 24) [31] (Tomlinson LJ; Gloster and David Richards LJ agreeing). The ALF had intervened in the appeal.

The judgments have, with respect, not clarified the law sufficiently, because the passage in fact suggests three potentially conflicting approaches:

- first, the Court eschewed any suggestion that it was requiring greater funder control;
- but, secondly, the Court also approved of the possibility that a funder's work in reviewing and monitoring litigation would alter the manner in which the litigation was conducted. Thus, some level of influence was endorsed; and
- thirdly, the Court appears to suggest that the indicia of impermissible control (i.e. champerty) might be its *effect*, rather than merely its extent – namely, whether the funder's involvement had 'interfer[ed] with the due administration of justice'.

The difficulty may be in the term 'control'. Clearly, the court approved of a funder having some input, and even exerting sufficient influence to alter the course of litigation. But it is not clear where the dividing line is between this conduct, and 'control'.

In Australia, a far greater level of control has been countenanced. In the leading case of *Campbells Cash and Carry Pty Ltd v Fostif Pty Ltd* (a case concerning the funding of a class action by a third party, acting for profit), the plurality recognised and accepted the pragmatic reality that a funder was likely to want to exert some control in the following terms:²⁷

... many people seek profit from assisting the processes of litigation. That a person who hazards funds in litigation wishes to control the litigation is hardly surprising.

²⁷. *Campbells Cash and Carry Pty Limited v Fostif Pty Limited* [2006] HCA 41; (2006) 229 CLR 386, [89] per Gummow, Hayne and Crennan JJ (Gleeson CJ agreeing).

This judgment was ‘widely interpreted as encouraging greater control by litigation funders in how a case is run’, and indeed led to IMF redrafting its funding agreements to seek more control over the litigation process.²⁸ Although Australian courts remain alive to the risk that non-party control may lead to the litigation being conducted in the interests of the funder, there is also recognition that there might be practical benefits, such as the introduction of a more commercial approach to litigation.²⁹

Practice

The position in practice is still more nuanced than the strict legal position might indicate. Australian funders more commonly promote their experience – and their ability to provide input to litigation – as a benefit of funding. In addition to the fact that control over litigation is more readily countenanced in Australia as a matter of law, a further reason might be that class actions form a substantial part of the Australian litigation funding industry, and a funder may be well-positioned to coordinate the class, including by conducting a bookbuild. In Australia, after the High Court sanctioned funder control in *Fostif*, market practice, and the terms of funding agreements, altered in response.³⁰ In recent years, large global funders have entered the Australian market. This has meant that the market has expanded, with a greater use of litigation funding as a risk management tool, and a greater use of portfolio finance.³¹ It seems that newer

²⁸ Julia May, ‘Lawyers Court Litigation Funding’ [2007] Business Review Weekly.

²⁹ *QPSX Limited v Ericsson Australia Pty Ltd (No 3)* [2005] FCA 933; (2005) 219 ALR 1, [54]-[55].

³⁰ May (n 28).

³¹ Burford, ‘5 Minutes With... Monique Cronin’ (17 December 2018) <<http://www.burfordcapital.com/blog/5-minutes-with-monique-cronin/>> accessed 5 May 2019. As to the general trends in the litigation funding market, see generally ‘Legal Finance Comes of Age in Australia’ (7 February 2019) <<http://www.burfordcapital.com/blog/legal-finance-comes-of-age-australia/>> accessed 5 May 2019.

entrants to the market are less likely to require control, and are more likely to promote their ‘ability to provide insights that drive more strategic decisions’, whilst ensuring that the terms of the funding agreement leave control in the hands of the claimant and lawyer.³²

In England, it has been observed that claimants often welcome the involvement of a funder in the litigation process, owing to their experience.³³ This may well be an aspect of the use of litigation funding as a ‘risk management’ tool. The level of influence or control exerted by a funder seems to vary amongst market participants, but the claimant does not relinquish control of the litigation.³⁴ For example, Therium describes itself as exerting ‘no influence’.³⁵ Burford states that all of its funding agreements make explicit that it does not control litigation. However, it may offer assistance, and it monitors litigation, for example, by being kept informed. Burford has explained that it is unnecessary for it to seek to control litigation, because it seeks to structure funding agreements so that the controlling parties ‘are incentivised to make rational decisions’.³⁶ In fact, claimants have total control even in relation to settlement.³⁷ It is clear, though, that a funder will, at a minimum be kept informed about progress.³⁸

³² Burford, for example, promotes itself as a ‘passive investor’ in claims: Burford (n 31).

³³ Rowles-Davies, (n 21) [2.130].

³⁴ *ibid* [1.32]-[1.34].

³⁵ Therium, ‘Frequently Asked Questions’ <<https://www.therium.com/frequently-asked-questions/>> accessed 10 May 2019.

³⁶ Burford, ‘Control: Addressing a common question about litigation finance’ (4 October 2017) <<http://www.burfordcapital.com/blog/control-addressing-common-question-litigation-finance/>> accessed 6 May 2019.

³⁷ *ibid*.

³⁸ Rowles-Davies, (n 21) [1.34]-[1.36], [1.40].

In both jurisdictions, there is limited empirical evidence as to what happens in practice. Such evidence as does exist predominantly arises from the context of Australian class action funding. In that context, in 2007, a partner of Australia's largest class action firm explained (in respect of a funding agreement with IMF which post-dated *Fostif*) that:³⁹

The cases are still run for the plaintiff, instructions still come from the plaintiff, but the terms say IMF will have day-to-day control. How do I interpret that? Any important decisions to be made in the litigation I will get from the client. But day-to-day I will be talking to IMF about what we're doing and what we're going to do.

Although class action practice is in an embryonic state in England, the practical position may be little different to Australia. For example, in the Volkswagen emissions group litigation, class members were required to appoint a committee to provide instructions to the solicitors.⁴⁰

In shareholder class actions, it is not uncommon for institutional investors to be members (so that the class might comprise both large institutional investors, and individuals with small shareholdings).⁴¹ One might have expected that institutional claimants would have both the expertise and motivation to provide instructions to the solicitors, reducing the need for input from the funder.

Nevertheless, a 2018 empirical study by Wayne of practices in funded Australian class actions – which involved interviews with three funders and one solicitors' firm –

³⁹ May (n 28).

⁴⁰ Slater + Gordon Lawyers, 'VW Emissions Action - FAQ' <<https://www.vwemissionsaction.com/faqs-for-the-vw-emissions-action-legal-claim>> accessed 29 May 2019.

⁴¹ Michael J Legg, 'Shareholder Class Actions in Australia - The Perfect Storm' (2008) 31 *University of New South Wales Law Journal* 669, 674-5; cf Michael Legg, 'Current Trends in Australian Shareholder Class Actions' (Presentation to Australian Insurance Law Association, Sydney, 19 August 2015), 26-30.

indicated that the involvement of funders varied, but was regarded as welcome by the solicitors. Waye reported that the principal of the solicitors' firm explained that some funders:⁴²

... chose to be actively involved in the strategic management of the action, particularly where the action was large scale, including so far as to be involved in the choice of barristers used during court hearings and the choice of class representatives. As a result of their expertise, the class law firm felt that active funders were generally better at formulating and driving strategy than class representatives whose lack of experience and interest in managing the action meant that they were often out of their depth and therefore unlikely to be in a position to give instructions that would benefit the class as a whole. Indeed, that principal found working with funders to be more positive than dealing with inexperienced, suspicious and difficult to work with solicitors representing corporate class members such as insurers. Nevertheless, in deference to the specialist legal expertise of the class law firm, funders were reluctant to be involved in purely legal tasks such as the drafting of pleadings and affidavits, managing discovery or briefing witnesses. Funders regarded their expertise as strategic and founded upon commercial judgment.

Thus, the class action solicitor regarded the solicitors acting for the insurer (one of the claimants in the class action) as 'inexperienced', 'suspicious' and 'difficult to deal with'.

As to the specifics of the funder's involvement, the funder and solicitor would communicate 'almost daily', and would monitor the proceedings through those communications as well as through any communications sent to class members.⁴³ Funders would question the litigation strategy, and would also scrutinise and, where necessary, dispute fees.⁴⁴

⁴² Vicki Waye, 'The Initiation and Operations Phase of the Litigation Funder - Class Action Law Firm Relationship: an Australian Perspective' (2018) 60 *International Journal of Law and Management* 595, 608.

⁴³ *ibid* 609-10.

⁴⁴ *ibid* 610.

Waye's survey indicated a divergence between how funders described their level control, and how much control they exercised in practice. In particular, Waye noted that most funders sought only 'the degree of control necessary to effectively monitor their investment'.⁴⁵ However, in practice some funders merely wished to receive periodic reports on the status of the litigation, while others were highly active in the conduct of the litigation, including 'monitoring proofing of key witnesses', attending 'strategy meetings with client and lawyer, and/or appointing lawyers'.⁴⁶

The disparity between how a particular funder describes their conduct, and what they actually do leads to two risks: (1) a failure of the claimant to understand how control will work in practice with a particular funder, and therefore (2) a mismatch of expectations between funder and claimant as to the level of control.

Regulatory options

The starting point is that third party control is not necessarily undesirable. First, some claimants may wish to cede some control to the funder: litigation is time-consuming and might divert attention away from more productive activities, and a funder is experienced in litigation.⁴⁷ Secondly, funder oversight has been recognised by courts to lead to benefits, such as the possibility that litigation will be conducted more efficiently, or to provide a 'check' on inappropriate litigation practices.⁴⁸ Thirdly, it is rational for funders to seek control litigation for the purpose of protecting their

⁴⁵ Vicki Waye, 'Conflicts of Interests between Claimholders, Lawyers and Litigation Entrepreneurs' (2007) 19 *Bond Law Review* 225, 253.

⁴⁶ *ibid* 253-4; see survey responses concerning control in Vicki Waye, *Trading in Legal Claims: Law, Policy & Future Directions in Australia, UK & US* (Presidian Legal Publications 2008), 284-7.

⁴⁷ Waye, 'Conflicts of Interests' (n 45); Waye, 'The Initiation and Operations Phase' (n 42) 608.

⁴⁸ *QPSX* (n 29); cf *Excalibur Ventures* (n 24).

investment.⁴⁹ Increased control might therefore decrease the cost of funding, because it decreases the risk to the funder that the client will behave irrationally. Fourthly, in the class action context, it might be practical (if not virtually necessary) for the funder to take a role in providing instructions, given the obvious difficulties in taking instructions from all class members, and the risks inherent in taking instructions only from the representative claimant or a committee of class members (namely, the risk that such claimants will further their own interests over those of the class, if and when they diverge).

Absent some principled reason for eschewing funder control (which was addressed and dismissed in Chapter 4), there seems to be no reason for preventing funder control – subject to a qualification identified below. However, the present difficulty in England is that the case law limits funder control (albeit it is not clear where, precisely, the line is drawn), and in both jurisdictions, there is a clear risk of some disparity between expectation and reality.

The problem of mismatch between expectation and reality is best dealt with either in the terms of the funding agreement, and also by the funder and/or solicitor providing concrete advice as to what level of involvement is expected by the funder.

The qualification is this: what happens if the interests of the funder and claimant diverge? This question also engages questions of the solicitor's role and ethical obligations, and as such is discussed in Chapter 11.

⁴⁹ As recognised by the majority of the High Court of Australia in *Fostif* (n 27).

Termination

It is theoretically possible that the funder might terminate the funding agreement in any one of four circumstances:

1. Because of unforeseen and unforeseeable events in the litigation – such as new facts coming to light which make the claim less prospective, or because unanticipated interlocutory steps or court rulings have affected the commerciality of the claim. It is not uncommon for funding agreements to permit the funder to terminate the agreement in the event of the claimant’s breach, or if the funder ‘reasonably ceases to be satisfied about the merits of the dispute’, or ‘reasonably believes that the dispute is no longer commercially viable’.⁵⁰ This circumstance presents little difficulty; it is appropriate and rational for litigation to cease where it emerges that the claim is unlikely to succeed, or is disproportionate.
2. Because of the claimant’s breach of the funding agreement, or the occurrence of matters within the claimant’s control – such as the discovery of new facts which were within the knowledge of the claimant, but which were not disclosed to the funder prior to entry into the funding agreement. Although these are matters within the claimant’s control, they are largely similar to category 1 above.
3. If the funding agreement gives a funder a right to terminate without cause.

⁵⁰

Adopting the descriptions used in clause 11.2 of the ALF, *Code of Conduct* (n 19).

4. In circumstances which constitute a breach of contract by the funder, for example in purported exercise of a right to terminate when no circumstances exist which would trigger that right. Such a circumstance would likely lead to a dispute between funder and claimant, which is addressed separately below.

Category 3 – terms enabling the funder to terminate at will – require further attention. Such a term has clear implications for the claimant, who may be unable to proceed with the litigation, and may also be liable for the costs of the defendant if the termination of the funding means that the claimant must discontinue. However, the risk that a funder will discontinue its funding is also an externality in economic terms: that is, the harm that it causes cannot be adequately accounted for in the initial contract between funder and claimant, because the harm affects third parties. The most obvious third party who will suffer is the defendant. If the claimant is unable to continue the proceedings owing to the funder's withdrawal, then the proceedings will be discontinued. If the claimant cannot afford to pay costs, then the defendant will have lost the cost of its legal expenses, which have now been thrown away, subject to the court's willingness to make a third-party costs order against the funder. Further, in all jurisdictions, there is also the cost to the civil justice system of proceedings being commenced without reaching a conclusion. It is wasteful of court resources, and unfair to other users of the civil justice system.

Regulatory options

There is merit in prohibiting any term which gives a funder a right to terminate without cause. This is the only way of avoiding the externalities described earlier. This is the

approach which is currently taken in the ALF Code and ALFA Guidelines,⁵¹ and ought to be mandated across the industry. The sophistication of the claimant does *not* serve to avoid or mitigate the risks.

The ALF Code and ALFA Guidelines permit the funder to terminate only in limited circumstances:⁵² i.e. where the funder (i) ‘reasonably believes that there has been a material breach’ of the funding agreement by the claimant; (ii) ‘reasonably ceases to be satisfied about the merits of the dispute’; or (iii) ‘reasonably believes that [it] is no longer commercially viable’. There are two good reasons for the second and third provision. First, if the prospects of success or recovery have diminished, then it would be disproportionate and wasteful of the resources of the parties and Court to continue. Secondly, a rational funder can be expected to be disincentivised to fund if they were obliged (by contract or regulation) to continue to fund in any event.⁵³

In England, the High Court in *Harcus Sinclair (a Firm) v Buttonwood Legal Capital Limited*⁵⁴ provided helpful guidance as to what it means for a funder to be ‘reasonably satisfied’ that the merits are no longer sufficient. In short, there is no specific process that the funder must adopt for the purpose of assessing the merits; rather:⁵⁵

The reasonableness of an estimate [concerning the prospects] is a purely substantive question, to be answered by an objective assessment of the available evidence against the background of the relevant legal rules and principles applicable to the claim. If the estimated figure is by that test

⁵¹ Discussed in Chapter 9.

⁵² See Chapter 9, footnotes 13 to 15 and accompanying text.

⁵³ Although compare Rachael Mulheron, ‘England’s Unique Approach to the Self-Regulation of Third Party Funding: A Critical Analysis of Recent Developments’ (2014) 73 *Cambridge Law Journal* 570, footnote 130 and the accompanying text.

⁵⁴ [2013] EWHC 1193 (Ch). See also *ibid* 589-90.

⁵⁵ *ibid* [43]; see also [38].

within the ambit of reasonableness, it matters not by what route or process it was reached: the result is all.

A funder may also terminate by accepting a repudiatory breach of the claimant;⁵⁶ the ALF Code and the ALFA Guidelines do not purport to modify the common law in that respect.

Adverse costs and security for costs

Adverse costs are treated very differently in England and Australia. In Australia, the litigation funder usually assumes responsibility for adverse costs as a matter of course. The ALRC has, in the context of class actions, recommended making this compulsory, on the basis that assuming this risk forms the ‘essential rationale’ for their receiving a percentage of any proceeds. In any event, third party costs orders are available, but there is no equivalent of the *Arkin* cap. The market for after-the-event insurance is growing in Australia,⁵⁷ and a funder may defray its risk by taking out such a policy.⁵⁸

In England, market practice is that the funder might assume responsibility for adverse costs, or might require that the cost of ATE insurance is factored into the cost of funding. As explained in Chapter 9, there is presently some uncertainty about the circumstances in which the *Arkin* cap applies.

A third-party costs order is an undesirable solution to the question of what to do about adverse costs. First, such an order is at the discretion of the court, placing the defendant in an unenviable position if the claimant is impecunious. Secondly, it

⁵⁶ *Vannin Capital PCC v RBOS Shareholders Action Group Ltd* [2018] EWHC 2821 (Ch), [96]-[113].

⁵⁷ ‘The Role of After the Event Insurance in Class Action Funding: 5 Years On’ (2019) <<https://www.kwm.com/en/au/knowledge/insights/the-role-of-after-the-event-insurance-in-class-action-funding-5-years-on-20190430>> accessed 5 August 2020.

⁵⁸ See, eg, *Clarke v Sandhurst Trustees Limited (No 2)* [2018] FCA 511, [5].

requires satellite litigation to determine the funder's liability. Thirdly, there is uncertainty about the scope of the rule. Fourthly, it involves externalities – namely, the increased cost and uncertainty for the defendant, and for the court system. Fifthly, the funder's capacity to pay any adverse costs depends on their capital adequacy. Even sophisticated claimants report difficulty in assessing this. Finally, there are externalities – whether a funder has assumed liability for adverse costs, or is well-capitalised, affects the defendant and potentially the court, but neither can protect themselves.

In relation to security for costs, there is a clear difficulty in the current Australian position, in that courts have recognised the need for a power to order security against a funder, but have been reluctant to amend court rules to this effect in the absence of legislative fiat. In this vacuum, the Federal Court has recently sought to use its inherent powers to impose security for costs on a funder. This suffers from the usual problems with judicial regulation identified in Chapter 9. It is particularly unsatisfactory in a federal system, because it is unclear whether other Australian courts will follow the lead of the Federal Court.

Regulatory options

The only way to address this problem would be to impose a requirement on funders that they assume liability for adverse costs and/or the cost of after-the-event insurance. On one view, this would have a tendency to increase the costs of litigation funding, as funders would need to recoup these additional liabilities. However, there are externalities involved, and it is not possible to protect the position of defendants by regulating the funder-claimant relationship alone. In practice, funders ought to be prepared for the risk of an adverse costs order, because of the possibility of a third-party

costs order (and are therefore likely to be including this in the cost of funding in any event, even in England). Mandating that the funder assumes this liability creates certainty for the funder as to the extent of its risks and liabilities.

The difficulty might be in avoiding any deterrent effect on funders who are asked to fund only part of the litigation expenses – such as where the claimant seeks funding for only the costs of expert evidence. There is no clear evidence that the removal of the *Arkin* cap in England would, in fact, have a chilling effect on the industry. But if that is a genuine difficulty, a more rational way to distribute adverse costs would be to impose a cap by way of *percentage*. For example, if a funder has funded 10% of the claimant’s costs, their liability for adverse costs would be limited to 10%. This would be consistent with the general justification for imposing adverse costs on an unsuccessful party: i.e. that it is in some measure reflective of the causative effect that the expenditure has had on the opponent’s legal fees.⁵⁹ Such a change would need to be effected via court rules.

As to the question of security for costs, the present difficulties in Australia could be rectified by a simple rule amendment, ideally in uniform terms across jurisdictions, of the sort which was contemplated by the Council of Chief Justices in 2009⁶⁰ – with legislative intervention if necessary. Indeed, it is very difficult to understand why such a change, which would clearly be to the benefit of defendants, has not already been made, at least at the Federal level, in circumstances where the present Government has been willing to engage in far more controversial law reform for the purpose of furthering the interests of defendants.

⁵⁹ *Commonwealth v Gretton* [2008] NSWCA 117, [121]; Adrian Zuckerman, *Zuckerman on Civil Procedure: Principles of Practice* (3rd edn, Thomson Reuters, Sweet & Maxwell 2013), [27.42].

⁶⁰ As discussed in Chapter 9.

Capital adequacy

If one were to review popular commentary on litigation funding, it would be rational to assume that litigation funding is an easy industry in which to make money – one in which funders can earn ‘windfall profits’ which might represent a substantial percentage of the claimant’s recovery. This disguises the true position, which is more complicated.

The first, and perhaps obvious, observation is that litigation funding is an industry that requires capital to be tied up for extended periods, and that wins and losses in litigation are all or nothing. It is unlikely that a funder will recover, say, 80% of its investment – it will either lose it entirely, or make a profit that may be (for calculation purposes) unrelated to the size of the investment. These features favour market participants who have access to substantial capital, and a diverse portfolio of cases; this, in turn, creates a barrier to participation in the market.

Indeed, in late 2015, Juridica Investments announced that it would not make any further investments, and would return its capital to investors. Juridica had been listed on the London stock exchange, and its chairman was Lord Daniel Brennan QC, a former chairman of the bar of England and Wales. Lord Brennan stated⁶¹

Both the Board of Juridica and its investment manager acknowledge that scale and diversity are now required in order to invest successfully in this asset class, which is not achievable under the Company’s existing structure.

The risk to a claimant is that if a funder suddenly runs out of funds, that may be fatal to its claims. In Australia, a class action brought against the Federal government

⁶¹ John Hyde, ‘Litigation Funder Pulls Plug on New Investments’ (*Law Gazette*, 18 November 2015) <<http://www.lawgazette.co.uk/news/litigation-funder-pulls-plug-on-new-investments/5052259.fullarticle>> accessed 5 March 2016.

by various claimants associated with the horseracing industry concerning the introduction of equine influenza into Australia was ultimately settled because the funder (Argentum Capital) failed partway through the litigation. The failure of Argentum left the claimants unable to proceed, and resulted in the lawyers for the class not being paid.⁶² Argentum was offshore, and the circumstances of its failure included allegations of fraud by a company which was said to be connected to the funder. Argentum was a member of the ALF in England and Wales, but withdrew from membership, and was ultimately delisted from the stock exchange.⁶³

The capital adequacy risk is likely to result in harm to the claimant, and also creates externalities.⁶⁴ The risk to the claimant and the risk of externalities are the same as if the funder terminated the agreement without cause, discussed earlier in the chapter.

It is difficult for a claimant to protect themselves against the capital adequacy risk. Unless the funder is publicly listed (such that its financial statements are publicly available), the claimant cannot know what the funder's financial position is; in any event, it may change over the period of the funding agreement. Significantly, it appears that even sophisticated repeat claimants cannot protect themselves against this risk. In the submissions to the ALRC enquiry, several pension (superannuation) funds identified that they considered themselves unable to assess properly the capital adequacy of funders.⁶⁵ Further, the capitalisation of a funder by itself is largely meaningless – a proper assessment of a funder's resources requires consideration of all

⁶² *Clasul Pty Ltd v Commonwealth of Australia* [2016] FCA 1119, [43], [45].

⁶³ 'Stock Exchange Delists Third-Party Litigation Funder' (2014) <<https://www.litigationfutures.com/news/stock-exchange-delists-third-party-litigation-funder>> accessed 5 August 2020.

⁶⁴ Walker (n 3) 101.

⁶⁵ Hesta, *Submission to Australian Law Reform Commission* (2018).

of their commitments. A claimant has no way of determining whether a funder's capital resources are notionally allocated to five claims or to 50.

In the literature produced by funders and funding brokers, two risks of the market stand out. First, there is the suggestion that some funding brokers are, in effect, purporting to be funders.⁶⁶ There is also the phenomenon of purported funders seeking out new claims, and then trying to raise capital to establish their litigation finance fund.⁶⁷ Both are potentially detrimental to clients, particularly if the purported funder does not disclose this practice to the claimant or lawyer, because (1) the funder might not raise the cash, leading to wasted time for the claimant, and (2) there is a risk that the purported funder will delay and prevaricate in agreeing terms, and therefore prevent the claimant from seeking funding elsewhere.⁶⁸

The other concern raised by the established funders is that many claimants fail to investigate, or even query, whether their funder has sufficient funds to see the litigation through to its end. In particular, it is observed that even if a funder has a pool of capital of, say, \$10 million, that is of little assistance to a claimant if the \$10 million is, in effect, supporting numerous claims. Thus, the suggestion is that claimants are not alive to risks of capital inadequacy, and the need to ensure that funds which are earmarked for their claim are ring-fenced.

⁶⁶ Rowles-Davies, (n 21) [4.09]; Burford, 'Using Litigation Finance: 12 Leading Lawyers Weigh In (Part II)' (25 October 2017) <<http://www.burfordcapital.com/blog/leading-lawyers-discuss-litigation-finance-2/>> accessed 6 May 2019.

⁶⁷ Rowles-Davies, (n 21) [4.22].

⁶⁸ *ibid* [4.24].

Regulatory options

Capital adequacy cannot be managed through regulation of the funder/claimant relationship. This is because it entails an externality – the risk to the defendant, and the justice system – so that even if a sophisticated claimant could avoid or mitigate the risk to themselves, the harm that it causes cannot be adequately accounted for in the initial contract between funder and claimant.

One option to protect against this risk would be impose requirements on funders to hold certain amounts in cash or readily liquidated assets, as in the English ALF Code. One risk is that this might increase the cost of litigation funding, because the rate of return on these safe assets will almost certainly be less than the rate of return on investing in litigation. Capital requirements therefore ought to be as limited as possible.

A further risk is that capital adequacy requirements might hinder competition in the litigating funding market, by acting as a barrier to entry.⁶⁹ On the other hand capital adequacy requirements will not be effective if they are negligible compared to a funder's commitments. There is, therefore, a good case for saying that capital adequacy requirements ought to be contingent on the size of the funder, rather than being constant across the industry.

More specifically, a capital requirement could be calculated by reference to (1) the funder's outstanding obligations in current litigation; and (2) the risk of adverse costs orders (which might be assumed, for these purposes, to be the same as the funder's expenditure). This might require review every, say, six or twelve months, in order to ensure currency.

⁶⁹ Timothy Lou, 'Into the Shadows: Shadow Banking and the Prudential Regulation of Litigation Funders' (2014) 14 Macquarie Law Journal 73, 86.

Another option would be to create an industry fund, which would satisfy the funding obligations of a collapsed funder. Equivalent schemes exist in the legal profession: in England,⁷⁰ and all Australian jurisdictions,⁷¹ all practitioners contribute to funds which compensate clients of lawyers in the event of fraud (for example). An industry-wide fund might be presently difficult to effect in a small industry – the failure of one could not be imposed on a small cohort. Further, if it were to be fair and fully effective, it would require some form of industry-wide regulation – as is seen with the Financial Services Compensation Scheme, and the legal professional schemes, where the industry as a whole (defined as including all those who enjoy some form of government-backed authorisation to carry on business in a given field) funds the scheme. For example, it would be unfair to require only members of the ALF to contribute to a fund that compensated clients of non-member funders, but on the other hand, a scheme that protected only the clients of the ALF would not be fully effective.

The Financial Services Compensation Scheme pays compensation to customers of failed finance firms, funded by the industry. Contributions are taken from all of those firms regulated by the FCA and the PRA, relative to the size of the firm. Levies are pooled by class, so that, for example, deposit firms' contributions are calculated and pooled separately to those of firms in general insurance provision – and compensation is also drawn from the corresponding pool.⁷²

Some funders (or, more accurately, one or more entities in the corporate structures of some funders) do, indeed, fall within the ambit of FCA regulation because,

⁷⁰ Solicitors Regulation Authority, *SRA Compensation Fund Rules* (2018).

⁷¹ See, eg, Legal Profession Uniform Law Application Act 2014 (Vic), Part 8; Legal Profession Uniform Law Application Act 2014 (NSW), Part 9.

⁷² Financial Services Compensation Scheme, 'How We Are Funded' <<https://www.fscs.org.uk/about-us/funding/>> accessed 1 March 2021.

for example, they are providing advice of a type that falls within the FCA's regulatory ambit.⁷³ However, funders are not regulated qua funder – the role of investing in litigation is not captured.

The FSA (the precursor to the FCA) indicated to Lord Justice Jackson in 2009 that it would not be able to take on the role of regulating for capital adequacy alone, and comprehensive regulation by the FCA would entail cost.⁷⁴ Since November 2018, claims management companies have been regulated by the FCA,⁷⁵ but funders do not fall within this (qua their funding role) because they are not providing advice, investigation or representation.⁷⁶

Disputes between funder and claimant

Disputes may emerge in any contractual relationship. However, disputes arising in the context of a litigation funding agreement have two features which may lead to particular risk: the potential for disparity of bargaining power between funder and claimant, and externalities. These can be illustrated by considering a dispute arising between funder and claimant over whether to accept a settlement offer.

First, the potential consequences to either party if the dispute cannot be resolved are extremely serious. The funder might threaten to withhold payments. The claimant might threaten to withhold cooperation, or to instruct solicitors to proceed in an

⁷³ FCA Handbook - Perimeter Guidance Manual (Release 32, Oct 2018); Financial Conduct Authority, 'List of Financial Activities we Regulate' (11 February 2019) <<https://www.fca.org.uk/firms/authorisation/how-to-apply/activities>> accessed 1 March 2021; see also Mulheron (n 53) 574.

⁷⁴ Jackson (n 2) Chapter 11, [3.2].

⁷⁵ Financial Services and Markets Act 2000 (Claims Management Activity) Order 2018/1253.

⁷⁶ And so fall outside *ibid* article 7.

uncommercial manner (for example, by rejecting a valuable offer of settlement). Either threat could ultimately harm both parties by jeopardising the prospects of the litigation.

Secondly, there is the potential for the defendant and the civil justice system to be affected (externalities). If a dispute between funder and claimant slows settlement discussions, that may affect the defendant: they incur costs as the delay progresses, and the delay may jeopardise the prospects of settlement. It might also affect the smooth running of the civil justice system: if a settlement is delayed, or rendered less likely, the proceedings will occupy more court resources. And, of course, there is a risk that a dispute between funder and claimant could produce satellite litigation.

A procedure for dispute resolution therefore ought to be included in the funding agreement. However, unlike the issue of, say, control, it is not sufficient merely that the funder and claimant agree. The content of their agreement is important. The dispute resolution process must be effective and efficient in practice, because of the externalities.

The types of dispute which might arise during litigation might be categorised both temporally, and by subject-matter. As to timing, a dispute which arises between funder and claimant during the course of litigation (as opposed to after its conclusion) has the potential to lead to externalities, in the form of affecting the progress of the claim. So, for example, if the funder and claimant disagree about whether or not to accept a settlement offer, that dispute has the potential to cause delay in the primary litigation. It is, therefore, critical that disputes arising during litigation are dealt with swiftly.

As to the subject-matter, a distinction may also be drawn between disputes about the conduct or settlement of litigation, for example – in which there may be no ‘right’

answer, but the funder and claimant must make a decision – and disputes which are simple contractual disputes about the operation of the funding agreement, such as whether the funder is required to pay a particular disbursement within the terms of the agreement, or the share of the proceeds to which the funder is entitled.

Regulatory options

There is a need for a clear procedure in the funding agreement for resolving disputes between funder and claimant which might arise in relation either to the operation of the funding agreement, or control of the litigation. As noted above, it is insufficient for the funder and claimant to agree about the dispute resolution procedure – it must meet objective standards in order to avoid the externalities described above.

A better option might be to adopt the approach in the ALF code of prescribing a particular dispute resolution procedure. This would remove the need for the funder and claimant to agree a process, and may also lead to uniformity in the industry.

In Australia, there is no prescribed dispute resolution procedure. In England, the prescribed process involves submitting the dispute to a senior counsel. There may be merit in having a centralised, industry-wide dispute resolution panel, in order to create consistency across the industry. Such a development would become increasingly proportionate as the industry expands.

Conclusion

This chapter has considered the six principal risks that arise from the funder-claimant relationship. This chapter assessed the root cause of each of those risks, using general and economic theory concerning regulation. In particular, the concept of market failure was introduced, and was later used to explain how the principal risks may be

ameliorated through regulation. Options for regulation, and their advantages and disadvantages, were discussed.

In the next chapter, I will consider the risks which arise from the relationship between lawyer, funder and claimant, and the implications for legal professional ethics.

CHAPTER 11 – REGULATING SOLICITORS’ PROFESSIONAL OBLIGATIONS

Introduction

Chapter 10 identified the risks arising from the relationship between funder and claimant, and possible options for regulation to mitigate or avoid these risks. This chapter addresses the question whether, and in what respects, the existence of litigation funding affects the relationship between solicitor and claimant.

It is common for commentators to suggest that the use of litigation investment is likely to have some implication for the relationship between lawyer and client, but there are diverse suggestions as to what that effect is likely to be. In this chapter, I consider the varieties of conflicts of interest and duty which might arise at different points in the litigation process. I address the gaps in existing regulation, and options for further regulation, including by comparing the position of solicitors who act for insured defendants.

This chapter focuses attention on the position of solicitors, rather than barristers. This is because, as will be seen, there are more points in the solicitor-client relationship at which the opportunity for conflict arises. Further, there are some duties – such as the duty to advise on costs – which are unique to solicitors. Finally, barristers almost always have a lay client (e.g. the claimant) as well as a professional client (i.e. the solicitor who instructs them). Consequently, barrister’s rules of ethics already have some provision for reconciling the duties owed to the lay client with the interest that a barrister has in maintaining a commercial relationship with their professional client.¹

¹ In Australia, the objects of the Legal Profession Uniform Conduct (Barristers) Rules 2015 include ensuring that barristers ‘act independently’, and ‘provide services of the highest standard unaffected by personal interest’: Legal Profession Uniform Conduct (Barristers) Rules

So, for example, there is a duty of independence, which might well address the relationship with funders in any event, or could easily be extended.

A further point of terminology arises. This chapter generally uses the terms ‘solicitors’ and ‘barristers’. However, judgments, some regulatory materials, and secondary literature on professional duties often use the term ‘lawyer’ to refer, compendiously, to both. From time to time in this chapter, the term ‘lawyer’ is used to mean a solicitor or barrister.

The relationship between funder and solicitor

Conventionally, the claimant approaches the solicitor first, and then seeks litigation funding. But there are many routes by which a solicitor and funder may come to be involved in litigation. In the Australian funding market, it is generally the case that a dual retainer, or a retainer solely by the funder, is uncommon, and the more usual

2015, s 3. the duty to the client includes that the barrister ‘... must promote and protect fearlessly and by all proper and lawful means the client’s best interests to the best of the barrister’s skill and diligence, and do so without regard to his or her own interest or to any consequences to the barrister or to any other person’: see s 35.

In England, the core duties of barristers include an obligation ‘to act in the best interests of each client’, to maintain their independence, and to ‘keep the affairs of each client confidential’: Bar Standards Board, *BSB Handbook* (Version 33, 2018), CD2, CD4 and CD6. The obligation of independence is also an aspect of a barrister’s duty to the court: rC3.

The duties to the client are intended to promote the outcomes that the best interests of the client ‘are protected and promoted by those acting for them’, that barristers do not accept instructions where there is a conflict between clients, or a conflict between their own interests and those of the client: oC11, oC12. (Client means simply ‘the person for whom you act’, any may include (depending on the context of the relevant rule) a prospective or a former client: Part 6, item 45).

More specifically, barristers must ‘promote fearlessly and by all proper and lawful means the client’s best interests... without regard to [their] own interests or to any consequences to [them]... [or] to any other person’: rC15.1-3. Further no other person may ‘limit [a barrister’s] discretion as to how the interests of the client can best be served’: rC15.4. See also rC20. The guidance confirms that a barrister’s duty is owed to their client, and not to a professional client: gC36.

Barristers are obliged not to accept instructions to act if they have previously accepted instructions which would impede upon their ability to act in the best interests of the prospective client: rC21.1. Nor may they act where there is a conflict of interest, or a real risk of such, between client and client (save where there is informed consent), or client and barrister: rC21.2-3. Nor may they act where the instructions ‘seek to limit [their] ordinary authority or discretion in the conduct of proceedings in court’: rC21.5.

situation is that the lawyer is retained solely by the claimants.² But in the class action context, the funder will often choose the lawyer, and set out the terms on which they will work, before the lawyer enters separate retainers with class members.³ It has been reported that in some circumstances a firm of solicitors will approach the funder on behalf of a group of claimants who are already its clients, in others a group of potential claimants will approach a funder in the first instance, and in others still the funder will approach a firm with a proposal to recruit class members.⁴ It appears that at least some funders, and some solicitors' firms, have a panel of solicitors or funders from which they will draw a partner for a piece of litigation.⁵ In class actions, it may be that the solicitors investigate the claim, and recruit claimants.⁶

Australian funders tend to promote the benefits for solicitors in restrained terms. For example, IMF, in identifying the benefits to solicitors of working with a funder, makes the point that '[t]he primary benefits of litigation funding are for the client', and, in respect of the solicitor's position, identifies only that it will enable an impecunious claimant to pursue litigation where it might not otherwise be able, and will aid cashflow for the solicitor in that it will assure prompt payment of fees.

Conversely, English funders are quite candid about the possibility of their interests aligning with the interests of a law firm. It is far more common for English funders to promote themselves as, in effect, partners to law firms. Specifically, English

² Wayne Attrill, 'The Regulation of Conflicts of Interest in Australian Litigation Funding' (UNSW Class Actions: Securities and Investor Cases Seminar, Sydney, 29 August 2013), 8-9.

³ Australian Law Reform Commission, *Integrity, Fairness and Efficiency—An Inquiry into Class Action Proceedings and Third-Party Litigation Funders (ALRC Report 134)* (2018), [4.72]-[4.73].

⁴ Vicki Wayne, 'The Initiation and Operations Phase of the Litigation Funder - Class Action Law Firm Relationship: an Australian Perspective' (2018) 60 *International Journal of Law and Management* 595, 603.

⁵ *ibid.*

⁶ *Kirby v Centro Properties Limited* [2008] FCA 1505, [4].

funders promote themselves as a source of new work for solicitors, and suggest ‘joint-pitching’ by the firm and the funder for new work. It is unknown whether this reflects different practices in the English and Australian funding markets, or whether it is simply the case that English funders are more overt in identifying the various benefits which might flow to a solicitor from having a funder fund their litigation (for example, because Australian funders and solicitors are subject to the commercial pressures described in Chapter 9).

Even where the solicitor is already retained, it seems clear in both jurisdictions that the identity of the lawyer is an important matter in the funder’s decision whether or not to fund.⁷ As such, even if the solicitor has approached the funder, having been selected and retained by the claimant, the funder still has a degree of commercial control over the identity of the solicitor.

The first step in considering the legal and ethical obligations of solicitors is to identify who is the client. As explained in Chapter 6, usual market practice is that the *claimant* retains the solicitor, and is therefore the solicitor’s client. It is uncommon for there to be a joint retainer (i.e., where the funder and claimant jointly retain the solicitor), or for the funder to have a separate retainer with the solicitors.⁸ An obvious exception is the class action context. In England, the lawyers will usually be nominated in the funding agreement between funder and claimant, or could be a party to that agreement.⁹

⁷ Waye, ‘The Initiation and Operations Phase’ (n 4) 604.

⁸ Attrill (n 2) 8-9; Nick Rowles-Davies, *Third Party Litigation Funding* (Jeremy Cousins QC ed, Oxford University Press 2014), Chapter 9.

⁹ Rowles-Davies (n 8) [1.29].

Thus, the claimant – and not the funder – is usually the solicitor’s client, and is the person to whom the solicitor owes their professional duties.

Defining the problem – conflicts of duty and conflicts of interest

Conflict problems for solicitors may be conceptualised as being divided into two categories: conflicts of duty and duty, and conflicts of duty and interest. Where litigation is funded by a third party, either (or both) forms of conflict might arise.

A conflict of duty and duty – or the potential for such – might therefore arise where the solicitor is also retained by the funder. This sometimes occurs in the class action context, but is otherwise uncommon. In this scenario, the solicitor will owe duties to the funder as client, and so the potential arises for a conflict of the duties owed to the two clients (funder and claimant).

A conflict of duty and interest usually entails that there is a conflict between the duty owed to the client and the solicitor’s own interest. Thus, even if the claimant alone is the solicitor’s client, there is, nevertheless, a potential for a conflict of duty (to the claimant) and the solicitor’s self-interest. In the litigation funding context, the solicitor’s interests can be thought of in two categories:

- First, the solicitor has their own, independent interests. Most obviously, a solicitor paid on an hourly basis might be said to have an interest in over-servicing, or in litigation being prolonged, in order to generate more fees. It is well-recognised that this interest exists whenever a solicitor is retained on

an hourly-fee basis.¹⁰ On the other hand, if fees are fixed or capped, it might be in the economic interest of the solicitor to under-serve.

- Secondly, it is rational to assume that the solicitor has an interest in maintaining good relations with the funder, who is ‘the repeat player who pays the lawyer’s fees’.¹¹ This interest might arise if a funder brings new claimants and matters to the firm, exerts influence as to the selection of the solicitor, enables litigation to proceed where it otherwise would not, and/or is likely to be a reliable payer. It might be expected that a commercial relationship may develop between the funder and the solicitor, even if the funder is not strictly the client. As a consequence, it might be in the solicitor’s interests to prefer the interests of the funder.

Any assessment of the risks of funding must compare the alternatives. In the absence of external funding, there are four alternative methods of payment:

First, the client may pay their own fees, on an hourly-billed basis, perhaps with a cap. As identified above, there is always a conflict of interest when a solicitor bills on an hourly basis, and the creation of a cap does not necessarily align their interest with that of the client.

¹⁰ See, eg, Kevin M Clermont and John D Currihan, ‘Improving on the Contingent Fee’ (1978) 63 Cornell Law Review 529; A Mitchell Polinsky and Daniel L Rubinfeld, ‘Aligning the Interests of Lawyers and Clients’ (2003) 5 American Law and Economics Review 165, 165.

¹¹ Michael Legg and US Chamber Institute for Legal Reform, *Litigation Funding in Australia: Identifying and Addressing Conflicts of Interest for Lawyers* (2012), 7. See also Vicki Waye, *Trading in Legal Claims: Law, Policy & Future Directions in Australia, UK & US* (Presidian Legal Publications 2008), 51 and 229; John Walker, ‘Policy and Regulatory Issues in Litigation Funding Revisited’ (2014) 55 Canadian Business Law Journal 85, 106.

Secondly, a conditional fees agreement might be used, which has always been permissible in some form.¹² Such an agreement does not avoid the usual conflict of interest which arises when a solicitor bills on an hourly basis, and it also means that the solicitor has a financial interest in the outcome of the litigation, which creates an additional ethical issue.

Thirdly, contingency fees may be used (where they are permissible). This again entails the solicitor having an interest in the outcome.

Finally, one might theoretically devise a system in which the cost of litigation was publicly funded.¹³ Whilst this avoids the ethical problems described above, it is inconceivable that such a system would be introduced by the state, given that the overwhelming trend in recent decades has been towards the privatisation of legal costs (as described in Chapter 5).

Any realistic system of paying legal fees therefore entails either that the solicitor will have some economic interest in the outcome of the litigation, and/or that the solicitor will have an economic interest which is opposed to that of the client. Both alternatives entail some ethical risk. It has proven impossible to devise a sustainable system for paying legal fees which avoids ethical risks all together.

Thus, whilst this chapter will consider the ethical risks of litigation funding, these ought not to be overstated. Instead, they ought to be compared to the ethical risks of the alternatives.

¹² Sir Jack IH Jacob, *The Fabric of English Civil Justice* (Stevens & Sons 1987), 279, observes that English law always permitted a speculative action, in which the lawyer agreed that payment would be made only following a costs order in favour of the client.

¹³ Wilmot-Smith proposes a system along these lines: Frederick Wilmot-Smith, *Equal Justice: Fair Legal Systems in an Unfair World* (Harvard University Press 2019), Chapter 9.

How and when might conflicts arise?

The nature of a conflict of interest and duty might be different at different stages of the litigation. There is also the possibility of an actual conflict when, for example, a duty to a claimant and a duty to a funder cannot be reconciled. Different conflicts are considered in the following section.

Entry into the funding agreement

A critical question is whether the solicitor acts for the claimant or the funder in settling the terms of the funding agreement. For a solicitor to act on both sides of a transaction always carries a risk of conflict: this is not a novel ethical problem.

In the case of litigation funding it would seem impossible for a solicitor to act on both sides with respect to entry into the funding agreement. Further, there would be intractable ethical difficulties with a solicitor acting for both a funder (who is conducting due diligence on the claimant's claim) and the claimant (who is the subject of the due diligence).

A particular problem arises in the context of class actions. Often, the funder selects the lawyer (and has a separate agreement with them). The funding agreement is then presented to potential claimants as, effectively, a standard form contract – there is little if any ability to negotiate terms. Claimants may be recruited via a website. Questions therefore arise as to the ability and/or obligation on solicitors to advise clients on entry into the agreement, or simply to inform them about the terms, particularly if there is a large class.

The problem is demonstrated by the allegations made in the Australian labour hire class action, discussed in the previous chapter. Whilst the solicitor and funder have denied any wrongdoing, the circumstances illustrate the potential difficulty of

providing advice on the content of litigation funding agreements to class action claimants (who may be numerous) especially when they are recruited via a website.¹⁴

Decisions about the conduct of the litigation

Throughout the course of litigation, decisions must be made about which causes of action to pursue and which to abandon, whether to appeal interlocutory judgments, and which barristers and experts to retain. Each decision might have consequences both for the cost of litigation (and its duration), and also for the prospects of success. As such, these sorts of decisions will affect the interests of both the claimant and the funder.

I explained in the previous chapter that the level of control ought to be agreed between parties prior to entry into the funding agreement. But this may not pre-empt all ethical dilemmas. Irrespective of the terms of the funding agreement, a funder who is being apprised of the progress of litigation is likely to express views about their preferred course of action. The ethical risk arises because a solicitor may have an interest in preferring the interest of the funder, with a view to enhancing the commercial relationship between solicitor and funder.

Secondly, if a funding agreement enables some degree of funder control, what is the solicitor to do if the funder gives instructions which are contrary to the claimant's interests (such as making an admission which may cause reputational damage to the claimant)?

Thirdly, one can also envisage circumstances in which the interests of the funder and claimant diverge. For example, if the solicitor learns a fact which would entitle the

¹⁴ For example, joining via a website was also the process for joining the Volkswagen class action in England: Slater + Gordon Lawyers, 'VW Emissions Action - FAQ' <<https://www.vwemissionsaction.com/faqs-for-the-vw-emissions-action-legal-claim>> accessed 29 May 2019, Q12.

funder to terminate, or becomes aware (in confidential circumstances) of matters which affect the merits or value of the claim. Is the solicitor obliged (or entitled) to reveal these matters to the funder?

Other risks, too, have been identified. It has been suggested that the presence of a third party funder may interfere with the lawyer's obligation to give independent advice.¹⁵ Walker suggests that a funder who seeks to exert too great control might not be kept in check by a lawyer (particularly in a class action, if the class is disparate and exercises little control).¹⁶

Silver argues that no such conflicts are likely to arise. He contends that the job of the lawyer is to advise; it is immaterial who makes the decision, and their reasons for following or rejecting advice. If the funding agreement entitles the funder to step into the claimant's shoes and provide instructions, then there is no ethical dilemma. On the other hand, if the claimant is constrained in its actions by the funder's pressure to act in a particular way, or threats of withdrawing funding, that is no different to other situations in which a claimant must make difficult decisions owing to financial constraints.¹⁷ Similarly, Wendel suggests that the interests of the funder, or the obligations between funder and claimant, are merely matters to be taken into account in providing independent advice to the client.¹⁸

One concern which is surprisingly infrequent in the literature is the possibility that a funder, as a repeat player in the litigation market, may exercise some level of de

¹⁵ See generally American Bar Association Commission on Ethics 20/20, *Informational Report to the House of Delegates* (2012), 15-18, 21-4.

¹⁶ Walker (n 11) 106.

¹⁷ Charles Silver, 'Litigation Funding versus Liability Insurance: What's the Difference?' (2014) 63 *DePaul Law Review* 617, 636-8.

¹⁸ W Bradley Wendel, 'A Legal Ethics Perspective on Alternative Litigation Financing' (2014) 55 *Canadian Business Law Journal* 133, 160.

facto control or influence over the lawyer, irrespective of the strict legal position, or the terms of the funding agreement.¹⁹

However, the risk of any divergence of interests in relation to settlement must be balanced against a countervailing benefit: the fact that the solicitor and funder share an interest in keeping the solicitor's costs down. Funders are well-placed to assess solicitor's fees, and report applying careful scrutiny to bills.²⁰

Settlement

Both the funder and the claimant have an interest in maximising the value of the claim. But their economic interest might diverge. First, if a matter proceeds to judgment, each will be out of funds for longer. But during this period, the funder will also continue to pay legal costs. Further, the opportunity cost of money might be different for the funder and claimant. Secondly, proceeding to judgment involves risk. The funder and claimant may have a different appetite for risk. Thirdly, the claimant might have a wish to be vindicated, or might resist the terms on which settlement has been offered. Alternatively, the claimant might wish to settle if it perceives there is some possibility of maintaining a commercial relationship with the defendant. Fourthly, the claimant and funder might simply take different views of the merits of the claim. Indeed, this possibility is implicit in the suggestion that funders bring a degree of commercial objectivity to the assessment of the merits of a claim.

For these reasons, settlement may present an opportunity for a dispute to arise between funder and claimant (an issue discussed in the previous chapter). However, it

¹⁹ It is referred to briefly by Elizabeth Chamblee Burch, 'Financiers as Monitors in Aggregate Litigation' (2012) 87 *New York University Law Review* 1273, 1320-1.

²⁰ Waye, 'The Initiation and Operations Phase' (n 4) 610.

also raises questions for the solicitor about how to reconcile the preferences and interests of funder and claimant.

Class actions

Class actions raise unique ethical issues. The Australian experience has been that funders play a significant role in organising the class, including identifying and recruiting claimants, and taking primary responsibility for the conduct of litigation. Further, funding is offered to class action claimants on standard terms, so that claimants may ‘take it or leave it’ – the inability of a claimant to negotiate terms, and the inequality of bargaining power, lead to a risk that uncommercial terms will be imposed. These difficulties have been identified earlier in the chapter. Indeed, where there is an open class, there is a possibility that the solicitors will have no retainer, or contact with, members of the class throughout the conduct of the action.

But funders might, in other ways, ameliorate conflicts in a class action context. Issacharoff identifies that a central problem with class action practice in the United States has been how to deal with agency costs: namely, the difficulty in ensuring that claimant lawyers act in the best interests of class members in circumstances where they are not monitored.²¹ Each of the attempted solutions has encountered difficulties because either they entail the appointment of a monitor who in turn generates agency costs of their own, or because the monitor is insufficiently incentivised or poorly placed to monitor.²² Issacharoff suggests that litigation funders may be well-placed to step into the breach as monitors of class-action proceedings – their interests are aligned with class members, as their return is contingent on the class’ recovery, their financial

²¹ Samuel Issacharoff, ‘Litigation Funding and the Problem of Agency Cost in Representative Actions’ (2014) 63 DePaul Law Review 561, 578.

²² *ibid* 579-82.

interest provides an incentive, and they are likely to be well-placed to get information about the proceedings.²³

These sorts of concerns are present in Australian class actions too, where it has been suggested that if a solicitor investigates the claim and recruits claimants, those claimants are ‘unlikely to be an effective superintendent of their action’, owing to the cost of doing so and the fact that an individual claimant may have a relatively small interest in the outcome.²⁴

Issacharoff demonstrates persuasively that the interest of funder and claimant may well be aligned in important respects. A funder who shares the claimant’s interests in minimising lawyer costs and maximising recovery, and is a powerful repeat player in the litigation industry, may well be a valuable ally.²⁵

However, there is also the potential for a funder and solicitor to align against the class’ interests. This possibility was raised in the course of resolving what to do about competing securities class actions against Centro Properties. Maurice Blackburn, the solicitors for one of the competing closed classes (‘Mr Kirby’s group’), agreed to the defendant’s suggestion that Mr Kirby’s group be opened to take in all class members, despite Maurice Blackburn having stated earlier in the proceedings that this

²³ *ibid* 582-3, drawing on Burch (n 19) 1316.

²⁴ *Kirby* (n 6) [30], see also [6].

²⁵ IMF (Australia) Ltd, ‘Submission to the Productivity Commission: Access to Justice Arrangements’ (2013) <<https://www.imf.com.au/docs/default-source/site-documents/bentham-imf-limited%27s-submission-to-the-productivity-commission-inquiry-into-access-to-justice-arrangements>> accessed 19 May 2015, [1.9] and [4.17]; see also Bentham IMF Limited, ‘Bentham IMF Litigation Funding Roundtable: Key Issues and Best Practices’ (2014) <<http://www.benthamimf.com/docs/default-source/default-document-library/bentham-report-final-10-01-14.pdf?sfvrsn=2>> accessed 19 May 2015, 7.

would make it harder to settle. Finkelstein J observed that any benefit to Mr Kirby's group was 'not immediately apparent',²⁶ and went on to state:²⁷

On the other hand, the proposal will benefit Maurice Blackburn and IMF. They are operating in a competitive market, in the case of Maurice Blackburn for the provision of legal services, and in the case of IMF for the provision of litigation funding. Keeping a competitor at bay by limiting his opportunities is a very desirable outcome. This, I think, has the potential to put Maurice Blackburn in an unenviable position; one where there is a risk that its personal interest might end up in conflict with its duty to its clients. True it is that Maurice Blackburn received instructions from Mr Kirby to accept [the defendant's solicitors'] proposal. But that may not be good enough. For one thing, there appears to have been no time for Mr Kirby to obtain independent legal advice. For another, I am not convinced that Mr Kirby's instructions to proceed are an adequate proxy for the wishes of the remaining group members (who number 955). In the circumstances, then, I cannot be sure of either Mr Kirby's or the remaining group members' wishes—possibly they might be dismayed to discover what is occurring.

Thus, the involvement of a funder in a class action has the potential to exacerbate conflicts, as well as to alleviate them.

What are the existing rules governing legal ethics in the funding context?

There is no regime in either Australia or England which regulates comprehensively the obligations of solicitors towards funders or funded claimants. There are, however, a variety of legal obligations which might be engaged, arising from a variety of sources of law:

- First, some of the (limited) regulation concerning litigation funding will indirectly affect solicitors.

²⁶ *Kirby* (n 6) [23].

²⁷ *ibid* [24].

- Secondly, the general law governing solicitors' professional obligations – such as codes of conduct, and fiduciary duties, will apply.
- In Australia, courts have used the doctrine of abuse of process to restrain solicitors and barristers from acting in particular circumstances in funded proceedings.

Rules specific to litigation funding

In neither England nor Australia is the position of the solicitor acting in funded proceedings directly regulated. But in both jurisdictions, the general regulatory provisions concerning litigation funding agreements contain some content which affects the position of solicitors.

Australia

In Australia, as was explained in Chapter 7, the Corporations Regulations 2001 (Cth) ('the Regulations') require funders to have in place practices for managing conflicts of interest. The application of the regulations is limited to those who are providing financial services in relation to litigation funding, and accordingly will *not* apply directly to lawyers acting as such.²⁸ Nevertheless, the Regulations affect the terms on which funders may retain solicitors. The Regulations, and the associated Regulatory Guidance issued by ASIC (which elaborates on the content of the Regulations), are theoretically applicable to all funding agreements. However, the content seems far more apposite to the class action context, as will be seen.

²⁸

Attrill (n 2) 10-11.

First, the Regulations require the funder to have a written procedure in place for managing conflicts in the event that a lawyer acts for both the funder and the claimant.²⁹

The Regulatory Guidance indicates that³⁰

... if there is no direct contractual relationship between the lawyers and each of the members, the funder should ensure that they engage the lawyers on terms that make clear that if there is a divergence of interests between the funder and the members, the lawyers must ensure that the members' interests are adequately protected.

The Regulatory Guidance acknowledges that where class members are the lawyer's clients, the potential for conflict is less.³¹ Importantly, in those circumstances, the Regulatory Guidance states that it is 'appropriate for the funder to give instructions to the lawyers and for the lawyers to consider these instructions in light of their obligation to the members'.³²

These rules mark a radical departure from the usual professional obligations of solicitors. First, where the claimant alone is the client, they expressly sanction a non-client (i.e. the funder) providing instructions. Secondly, where the funder alone is the client, the rules contemplate that the lawyer nevertheless has obligations to a non-client – i.e. the claimant.

Secondly, the Regulations require that there be procedures in place to deal with the situation in which there is any pre-existing relationship between any of the funder, lawyers and claimants.³³ In short, ASIC expects that the parties will either be independent of each other, or that there should be disclosure of pre-existing

²⁹ Corporations Regulations 2001 (Cth), reg 7.6.01AB(4)(d)(v).

³⁰ Australian Securities and Investment Commission, *Litigation Schemes and Proof of Debt Schemes: Managing Conflicts of Interest (Regulatory Guide 248)* (2013), RG 248.77.

³¹ *ibid* RG 248.78.

³² *ibid* RG 248.79.

³³ Corporations Regulations 2001 (Cth), reg 7.6.01AB(4)(d)(vi).

relationships (whether present, or existing in the previous two years), whether in the form of a financial benefit, or specified forms of relationship between senior personnel.³⁴

Thirdly, ASIC has acknowledged that particular issues of conflict may arise in the context of settlement. On one hand, its regulatory guidance indicates that both the funder and the lawyers are well-placed to know whether a settlement proposal is in the best interests of the claimant; but on the other, it is ‘concerned about the potential for the funder and lawyers to prefer their own commercial interests over those of the members’, or for the settlement to be in the interest of the lead claimant only.³⁵ ASIC has nevertheless indicated that court oversight of settlement provides sufficient protection.³⁶ However, this will obviously apply only in the situation in which there is a class action. Where proceedings are settled before they are issued, then ASIC expects that the fairness of the settlement agreement will be assessed by the counsel which has been engaged, adopting the approach taken by court.³⁷ ASIC’s guidance on this third point is silent on the position where the funding agreement does *not* deal with a class action. This is a serious omission.

In summary, the limits of these rules are, first, that they are not directed to lawyers as such, and do not purport to make clear the lawyer’s obligations. Rather, these rules are directed to the position of funders, and their effect (if any) on lawyers is secondary only. Secondly, the rules seem most apt – and in some cases, seem to be limited to – the position of lawyer acting in funded class actions.

³⁴ ASIC (n 30) RG 248.80-85.

³⁵ *ibid* RG 248.89.

³⁶ *ibid* RG 248.90.

³⁷ *ibid* RG 248.91-98.

England

The Code of Conduct of the Association of Litigation Funders ('the Code') contains some limited provisions which regulate funders' dealings with lawyers. They are directed solely towards funders.

First, the funder is required to take 'reasonable steps' to ensure that the claimant has taken independent advice on the terms of the funding agreement.³⁸ The funder must 'not take any steps that cause or are likely to cause the Funded Party's solicitor or barrister to act in breach of their professional duties' and must 'not seek to influence the Funded Party's solicitor or barrister to cede control or conduct of the dispute to the Funder'.³⁹

Secondly, the Code contains some restraints on the terms of the litigation funding agreement. Relevantly to the solicitor, the agreement must state whether, and how, the funder or a related party may 'provide input to the Funder Party's decisions in relation to settlements'.⁴⁰ If the agreement *does* provide for the funder to have some input to the settlement decision, then the funding agreement must also contain a dispute resolution clause in the prescribed form – namely, that a binding opinion will be obtained from a silk 'who shall be instructed jointly or nominated by the Chairman of the Bar Council'.⁴¹

The Code also expressly preserves a funder's entitlement to conduct 'appropriate due diligence' before funding, and during litigation, 'including but not limited to analysis of the law, facts, witnesses and costs relating to a claim, and

³⁸ Association of Litigation Funders, *Code of Conduct for Litigation Funders* (2018), [9.1].

³⁹ *ibid* [9.2] and [9.3].

⁴⁰ *ibid* [11.1].

⁴¹ *ibid* [13.2].

including regularly reviewing the progress of the litigation'.⁴² This rule is new to the 2018 edition of the rules,⁴³ and appears to have been responsive to the judgments in *Excalibur*.

An important benefit of the Code is that it requires control issues to be addressed in the funding agreement, and there is also a prescribed dispute resolution clause. The Code prevents funders from taking steps to cause the solicitors to cede control of the litigation, but it does not identify specifically the border between permissible and impermissible involvement. This is unsurprising, given the Code's apparent reference to the *Excalibur* judgments, which did not give clear guidance on this point.

Fiduciary duties

It is trite law that solicitors owe fiduciary obligations to their clients.⁴⁴ The paradigm fiduciary obligations are the duty to avoid conflicts of interest, and the duty not to obtain an unauthorised benefit from the position of fiduciary. But, the extent of a solicitor's fiduciary obligations depends critically on the scope of the retainer.⁴⁵

⁴² *ibid* [18].

⁴³ The previous version was dated 14 January 2014: Association of Litigation Funders of England and Wales, *Code of Conduct, 14 January 2014* (2014).

⁴⁴ *Maguire v Makaronis* (1997) 188 CLR 449.

⁴⁵ *Beach Petroleum NL v Abbott Tout Russell Kennedy* [1999] NSWCA 408; (1999) 48 NSWLR 1, [188].

General conduct rules

Australia

The Australian Solicitors' Conduct Rules⁴⁶ identify the general duties owed by all Australian solicitors.⁴⁷ Amongst the 'fundamental ethical duties' is the requirement that a solicitor 'avoid any compromise to their integrity and professional independence'.⁴⁸ In the commentary, it is observed that solicitors should, 'as a matter of course, consider and advise clients of the possible availability of legal aid where appropriate'.⁴⁹ The rules require solicitors to avoid conflicts between current and former clients, two current clients, and between a client and the solicitor's own interests, and make separate provision for each situation of potential conflict.⁵⁰

In relation to conflicts between two current clients, the rules provide that a solicitor must not act 'where the clients' interests are adverse and there is a conflict or potential conflict of the duties to act in the best interests of each client', unless each client is aware that the solicitor acts for the other and has given their informed consent to the arrangements.⁵¹ In respect of conflicts between the solicitor's own interests and those of their client, the rules provide relevantly that a solicitor 'must not act for a client

⁴⁶ Law Council of Australia, *Australian Solicitors' Conduct Rules* (2015).

⁴⁷ The rules are binding on all solicitors in Australia: *ibid*, rule 1.1. The rules are not comprehensive in identifying solicitors' ethical obligations; there are also statutory and common law principles.

⁴⁸ *ibid*, rule 4.1.1 and 4.1.4 respectively.

⁴⁹ Law Council of Australia, *Commentary to the Australian Solicitors' Conduct Rules* (2013), commentary to rule 4.

⁵⁰ *ibid*, rules 10, 11 and 12 respectively.

⁵¹ *ibid*, rules 11.2 and 11.3.

where there is a conflict between the duty to serve the best interests of a client and the interests of the solicitor or an associate of the solicitor'.⁵²

In respect of confidentiality, the rules provide that a solicitor must not disclose a client's confidential information except where (relevantly for presently purposes) 'the client expressly or impliedly authorises disclosure' or 'the solicitor is permitted or is compelled by law to disclose'.⁵³ It is possible to infer an implied authority from the nature of the retainer.⁵⁴

Australian rules of conduct are expressed at a high level of generality, in terms of broad principles rather than specific guidance (in contrast to the English rules, which are addressed below). But even at this level of generality, there are topics which are not addressed – in particular, obligations of disclosure concerning fee arrangements.

England

The SRA Handbook identifies, amongst the mandatory principles applicable to solicitors, that solicitors 'not allow [their] independence to be compromised', and 'act in the best interests of each client'.⁵⁵ Independence 'means your own and your firm's independence, and not merely your ability to give independent advice to a client', so

⁵² *ibid*, rule 12.1. An associate is defined in the Glossary as:

- (a) a partner, employee, or agent of the solicitor or of the solicitor's law practice;
- (b) a corporation or partnership in which the solicitor has a material beneficial interest;
- (c) in the case of the solicitor's incorporated legal practice, a director of the incorporated legal practice or of a subsidiary of the incorporated legal practice;
- (d) a member of the solicitor's immediate family; or
- (e) a member of the immediate family of a partner of the solicitor's law practice or of the immediate family of a director of the solicitor's incorporated legal practice or a subsidiary of the incorporated legal practice.

⁵³ *ibid*, rules 9.2.1 and 9.2.2. The other exceptions are not relevant to the position as between client, solicitor and funder.

⁵⁴ *ibid*, commentary to rule 9.

⁵⁵ Solicitors Regulation Authority, *SRA Handbook* (2018), 1.3 and 1.4.

that a solicitor may not (for example) permit a third party to control their practice.⁵⁶

The obligation to act in the best interests of each client includes ‘most importantly’ the duties concerning confidentiality and avoidance of conflicts.⁵⁷

In respect of client care, solicitors are required to achieve the following outcomes (amongst others):

- ‘only enter into fee agreements with [their] clients that are legal, and which [they] consider are suitable for the client’s needs and take account of the client’s best interests’,⁵⁸ and
- ensure that ‘clients are in a position to make informed decisions about the services they need, how their matter will be handled and the options available to them’.⁵⁹

The ‘indicative behaviours’ include:

- ‘explaining any limitations or conditions on what [they] can do for the client, for example, because of the way the client’s matter is funded’;⁶⁰
- ‘considering whether you should decline to act or cease to act because you cannot act in the client’s best interests’;⁶¹
- ‘discussing how the client will pay, including ... whether the client has insurance that might cover the fees, and whether the fees may be paid by someone else such as a trade union’;⁶² and

⁵⁶ *ibid*, 2.7.

⁵⁷ *ibid*, 2.8.

⁵⁸ *ibid*, O(1.6).

⁵⁹ *ibid*, O(1.12).

⁶⁰ *ibid*, IB(1.5).

⁶¹ *ibid*, IB(1.7).

⁶² *ibid*, IB(1.16).

- ‘where [they] are acting for a client under a fee arrangement governed by statute, such as a conditional fee agreement, giving the client all relevant information relating to that arrangement’.⁶³

Notably, therefore, there are obligations concerning other forms of funding arrangements, but not litigation funding. The outcomes will *not* be achieved where (amongst other things) the solicitor is ‘acting for a client when instructions are given by someone else, or by only one client when [they] act jointly for others unless [they] are satisfied that the person providing the instructions has the authority to do so on behalf of all of the clients’.⁶⁴

In respect of conflicts of interest, a solicitor may never act ‘where there is a conflict, or a significant risk of conflict between [the solicitor] and [their] client’.⁶⁵ Where there is a conflict or a significant risk of such between two or more clients, then the solicitor must not act for both or all unless one of the exceptions applies.⁶⁶ One exception arises where the clients have a substantially common interest, which is:⁶⁷

a situation where there is a clear common purpose in relation to any matter or a particular aspect of it between the clients and a strong consensus on how it is to be achieved and the client conflict is peripheral to this common purpose.

Even here, a solicitor may only act where all clients have given their fully informed consent, and the solicitor is satisfied that it is in the clients’ best interests to act for all and that the benefits of doing so outweigh the risks.⁶⁸

⁶³ *ibid*, IB(1.17).

⁶⁴ *ibid*, IB(1.25).

⁶⁵ *ibid*, introduction to Chapter 3; see also O(3.4).

⁶⁶ *ibid*, introduction to Chapter 3; see also O(3.5).

⁶⁷ *ibid*, Glossary.

⁶⁸ *ibid*, O(3.6).

The protection of a client's confidential information is described as a 'fundamental feature' of the relationship.⁶⁹ It takes priority over the duty of disclosure to other clients (that is, the duty to disclose information which is within the solicitor's knowledge and is material to that other client's matter).⁷⁰ Amongst the outcomes which solicitors must achieve are not to act for potential client A where the solicitor has confidential information about client B which is relevant to A, and the interests of A and B are adverse. The only exceptions are where there is fully-informed consent of B, or safeguards have been put in place.⁷¹ But the notes indicate that it may be difficult to establish the necessary safeguards where 'the clients are not sophisticated users of legal services'.⁷² No criteria are given for identifying a sophisticated user of legal services.

The SRA Handbook also regulates the situation where a solicitor has some arrangement with a third party, by which the third party introduces business to the solicitor and/or shares the solicitor's fees.⁷³ In respect of such agreements, a solicitor must ensure that the solicitor's 'independence and... professional judgment are not prejudiced by virtue of any arrangement with another person'.⁷⁴ Amongst the indicative behaviours are that the solicitor 'only [enters] arrangements with reputable third parties and monitoring the outcome of those arrangements to ensure that clients are treated fairly'.⁷⁵ An arrangement is broadly defined as⁷⁶ 'any express or tacit agreement between you and another person, whether contractually binding or not.'

⁶⁹ *ibid*, introduction to Chapter 4.

⁷⁰ *ibid*, introduction to Chapter 4, and see also O(4.3).

⁷¹ *ibid*, O(4.4).

⁷² *ibid*, notes to Chapter 4.

⁷³ See generally *ibid* Chapter 9.

⁷⁴ *ibid*, O(9.1).

⁷⁵ *ibid*, IB(9.1).

⁷⁶ *ibid*, Glossary.

By comparison with the Australian rules of conduct, the SRA Handbook contains extremely detailed guidance about the standards expected of solicitors, and the sorts of behaviour which will fall inside or outside the scheme. But it does not deal with the position of a third-party funder. Further, there are some rules where it might be said that a funder might fall within the spirit or intention of the rule, but not within its express terms – such as the rule governing solicitors who enter into third party agreements, the duty to explain CFAs and other fee agreements governed by statute, and the duty to discuss how a client will pay for litigation.

Taking that last duty as an example, it has been argued that the obligation of solicitors to provide clients with information about costs and payment options might include a duty to inform the client about funding.⁷⁷ However, the English rules seem directed to considering the availability of a source of funds to which the claimant is already entitled.⁷⁸ It seems unlikely that there is a specific obligation to raise with a client the possible availability of litigation funding, although the matter is not beyond doubt.⁷⁹

Case law

In Australia, a series of judgments delivered by Victorian Supreme Court and Court of Appeal have used the doctrine of abuse of process to prevent a solicitor and counsel from having an interest in the litigation funder. In *Bolitho v Banksia Securities (No 4)*,⁸⁰ the defendant to a class action sought to restrain the solicitor and senior counsel

⁷⁷ Rowles-Davies (n 8) [1.58]-[1.59]; Lisa Bench Nieuwveld and Victoria Shannon Sahani, *Third-Party Funding in International Arbitration* (2nd edn, Kluwer Law International 2017), 49.

⁷⁸ *Sarwar v Alam* [2001] EWCA Civ 1401; [2002] 1 WLR 125, [45] (per curiam); *Jackson and Powell on Professional Liability* (Mark Cannon, Hugh Evans and Roger Stewart eds, 8th edn, Sweet & Maxwell 2017), [11-182].

⁷⁹ Although see a contrary argument by Rowles-Davies.

⁸⁰ *Bolitho v Banksia Securities Limited (No 4)* [2014] VSC 582.

for the class from acting. The class action was funded, and the funder was entitled to share up to 30 per cent of the proceeds in the event of success. Entities associated with the solicitor held 45 per cent of the shares in the funder, and a company associated with the wife of the senior counsel held another 45 per cent of the shares.⁸¹

Ferguson JA observed that the court had an inherent jurisdiction to restrain a lawyer from acting ‘to ensure the due administration of justice and to protect the integrity of the judicial process’.⁸² Her Honour considered that the solicitor and barrister ought to be restrained from acting because the arrangements would be perceived by a ‘fair-minded, reasonably informed member of the public’ as an attempt to evade the ban on contingency fees and the 25% limit on uplift fees in conditional fee arrangements.⁸³ But her Honour also went on to say that:⁸⁴

The position might be different in circumstances where the lawyer’s interest was more modest, but here the 45 per cent interest and the quantum of the claim take it beyond something that might be seen as insufficiently significant to give rise to concern....

The judgment does not, unfortunately, provide clear guidance for solicitors and barristers. First, her Honour appears to have regarded as critical (1) the fact that the interest in the funder was 45% and (2) the quantum of the claim. It is obviously not clear where the line would be drawn in future cases. Secondly, it is not clear whether the solicitor having an interest in the funder was undesirable per se, or was only

⁸¹ *ibid* [7]–[8].

⁸² *ibid* [16(a)].

⁸³ *ibid* [50]–[51]. Her Honour observed that a further difficulty arose because of the ‘number of hats’ the solicitor wore: at [53] (the solicitor had also been retained on a conditional costs agreement: at [6]). As to the application of this reasoning to the senior counsel (who was also restrained), see at [61].

⁸⁴ *ibid* [52].

problematic because it involved evading, in effect, the regulations which limited conditional fees and banned contingency fees.

Is further regulation of solicitors' obligations necessary?

Why are solicitors regulated at all?

Regulation may be justified by either the need to correct various market failures (including inequality of bargaining power), or the need to promote the social good of consumer protection.

These two justifications have been observed in the specific context of regulation of the legal profession.⁸⁵ It is accepted that there exist various market failures in the market for legal services, which justify regulation.⁸⁶

But, importantly, there is a further consideration. As discussed in Chapter 3, an aspect of the social good is the need to secure the proper administration of justice, including upholding the rule of law, and maintaining public confidence in the profession. In this respect, it has been said that⁸⁷

The liberal professions justify regulation of their activities by invoking quality control, promoting high standards of access, ensuring effective and transparent competition, and the like. The legal profession is particularly closely regulated on the grounds that such regulations, by contributing to the good administration of justice, uphold the rule of law. The lawyer is granted a number of important privileges. ... The counterpart of these privileges is that the legal profession is strictly regulated. Lawyers must respect, in letter and in spirit, detailed standards that are commonly codified in professional regulations.

⁸⁵ Frank H Stephen, *Lawyers, Markets and Regulation* (Edward Elgar 2013), chapter 2.

⁸⁶ *ibid* 12.

⁸⁷ Ian S Forrester, 'Where Law Meets Competition: Is Wouters Like a Cassis de Dijon or a Platypus?' in Claus-Dieter Ehlermann and Isabela Atanasiu (eds), *European Competition Law Annual 2004: The Relationship Between Competition Law and the (Liberal) Professions* (Hart Publishing 2006), 275.

In the specific context of the legal profession, this idea is commonly expressed by commentators in terms of a social contract, pursuant to which the legal profession is permitted certain privileges (self-regulation; exclusivity over particular areas of practice) in exchange for protecting the public interest in access to an honest, competent legal profession.

In Chapter 5, I explained that the ethical obligations placed on lawyers may be explained, in part, by the special role that lawyers play in the system of justice – particularly in the adversarial system, where lawyers have substantial control over proceedings. The need to ensure scrupulous behaviour by lawyers therefore has two dimensions: protection of the client, and a systemic aspect, in which the honesty and integrity of lawyers – as well as the appearance of such – is a necessary aspect of the adversarial system of justice. As a consequence, a lawyer cannot contract out of their ethical obligations, even where their client is sophisticated and well-informed.

In considering whether further regulation of solicitors' obligations is necessary, it is therefore insufficient to consider solely the protection of the client. It is also necessary to consider the integrity of the profession, and the appearance of such.

What problems currently exist?

There is limited evidence that funded claimants are, presently, being adversely affected by ethical breaches by their lawyers, and the problems which have arisen have tended to cluster in class actions.⁸⁸ It is not clear whether this is because class actions raise

⁸⁸ In its interim report Australian Law Reform Commission, *Inquiry into Class Action Proceedings and Third-Party Litigation Funders (DP 85)* (Discussion Paper, 2018), the ALRC identified various instances of legal ethical problems or risks in the context of class actions. In some of these, the problem was either specific to the class action context, or was *not* unique to the funding context. Specifically, ethical problems identified included the fact that the existing provisions concerning class actions did not adequately deal with the obligations of solicitors towards group members (see [4.50]), a report of a single instance of a solicitor commencing a class actions when they had not obtained proper instructions and appeared to be insufficiently

unique In this context, there have been reports of specific problems arising (as described earlier in this chapter) – such as allegations that solicitors have failed to explain the terms of a funding agreement to their clients, or solicitors having a financial interest in the litigation funder. In addition to these, in its interim report on class actions and litigation funding, the ALRC reported that it had ‘heard of pressure being placed on solicitors for representative plaintiffs by litigation funders to settle class action proceedings prematurely’, which would obviously be in breach of the existing regulation of funders,⁸⁹ and had also ‘heard of funders withholding confidential settlement offers from the representative claimant and solicitors, and of ‘shopping’ for counsel to give a favourable opinion to the Court as to the appropriateness of the proposed settlement’.⁹⁰

Nevertheless, there are five reasons why further regulation of legal ethics may be necessary. First, it has been argued that the general rules concerning solicitors’ duties and their obligations in situations of conflict may not be sufficient to deal with the particular conflict situations which arise where proceedings are funded.⁹¹ Further, as explained above, there are numerous legal ethical rules for which it is unclear whether and how they ought to apply in the litigation funding context (such as the obligation to discuss costs).

experienced or resourced to deal with a class action (see [4.52]), a report of a law firm applying (but then withdrawing its application) to have a class action funded by a related entity (see [4.63]) and a case in which the court prevented, on the ground of abuse of process, a class action from proceeding in circumstances where the lawyer for the lead claimant had an interest in the funder (at [4.63]). The risk of solicitors firms taking on class actions when insufficiently experienced to do so was considered to be heightened by the great increase in the number of firms who had commenced class actions in the period 2005 to 2017 (see [4.53]-[4.54]).

⁸⁹ ASIC (n 30).

⁹⁰ ALRC, *Inquiry* (n 88) [4.35].

⁹¹ *ibid* [4.51].

Secondly, in the absence of clear regulatory standards, it is possible (if not likely) that courts will be required to develop principles to apply to conflict situations as they emerge. The series of Victorian judgments concerning the question whether a solicitor may have an interest in a litigation funder is an example of such judicial regulation.⁹² The difficulties with judicial regulation were explained in Chapter 7. It would be desirable to pre-empt the need for judicial regulation by creating clear standards in advance.

Thirdly, given the uncertainty of application of some existing rules, and the difficulty of using court-developed principles to resolve ethical issues, it is arguable that regulation might assist in promoting the integrity, and appearance of integrity, of the profession. The importance of the integrity of the legal profession, and the appearance of such, were discussed in Chapter 3.

Fourthly, there might be consumer protection benefits to further regulation. For example, if there were clear guidelines as to whether a solicitor was obliged to discuss funding with their client, that would avoid any uncertainty as to a solicitor's obligations, and would also tend to create a uniformity of approach between different solicitors.

Fifthly, at present, the litigation funding market is still relatively small, and the extent to which it is regulated is unsettled and under periodic review. As discussed in Chapter 9, there is evidence from the Australian class action funding market to indicate that these features have created commercial pressures on both funders and solicitors to act scrupulously. Thus, the fact that ethical problems are not, as yet, widespread, is not good evidence that they might not emerge.

⁹² Discussed earlier, in the text accompanying footnote 80.

A comparison with insurance

In considering how conflict situations may be dealt with in practice, the position of solicitors acting for insured defendants is instructive. This is because it is common for an insurer to take over conduct of litigation, despite not been a party to it.

It has been suggested that, insofar as there are ethical difficulties with litigation funding, they might be resolved by analogy with the approach taken in insurance cases.

Solicitors' obligations in the insurance context

An insurer may take over the conduct of a party's litigation in two contexts.

Subrogation

First, where a person has suffered a compensable loss at the hands of another, and is also insured in respect of that loss, the insured's claim against the wrongdoer may be taken over by the insurer through the application of the doctrine of subrogation. In both Australian and English law, subrogation is⁹³

... a process by which one party is deemed to have been substituted for another, so that he can acquire and enforce the other's rights against a third party for his own benefit. It is often said that a subrogated claimant 'stands in the shoes' of the party whose rights he is deemed to have acquired.

There are several established categories of relationship in which the doctrine of subrogation applies, one of which is insurer and insured. In the insurance context, in simplified terms, the effect of subrogation is that if (and only if) the insurer completely indemnifies the insured for the loss it has suffered at the hands of a third party, it will

⁹³ Charles Mitchell and others, *Subrogation: Law and Practice* (rev edn, Oxford University Press 2007), [1.01].

‘succeed[] to the insured’s cause of action against the third party’.⁹⁴ The doctrine therefore operates (1) to avoid any loss to the insurer in circumstances where it ought to be borne by the third party, and (2) to avoid the insured obtaining a double recovery.⁹⁵ Importantly, the insurer is not necessarily entitled to the entirety of the fruits of any litigation against the third party; rather, the insurer’s rights against the third party are limited to indemnifying the *insurer* for the loss it has suffered, and any excess recovery must be provided to the insured.⁹⁶

Any claim is brought in the name of the insured,⁹⁷ although the insurer will conduct litigation (including by instructing solicitors).⁹⁸ The doctrine of subrogation provides a well-recognised exception to the doctrine of maintenance and champerty, because it is accepted that the insurer has a legitimate interest in the litigation in question.⁹⁹

Litigation funding is substantially different; the funder does not succeed to the claimant’s cause of action, does not fully indemnify them for their loss, and shares in the fruits of the litigation in a manner which entails profit (rather than mere discharging the funder’s own ‘loss’, or expenditure on the litigation). For that reason, the doctrine of subrogation – and the rules which have developed concerning the obligations of the

⁹⁴ *Sydney Turf Club v Crowley* [1971] 1 NSWLR 724, 734; J D Heydon, M J Leeming and P G Turner, *Meagher, Gummow and Lehane's Equity Doctrines and Remedies* (5th edn, LexisNexis Butterworths 2015), [9.210], [9.250], [9.255]. See also Mitchell (n 93) [10.40]-[10.60] as to the preconditions for the operation of subrogation in the context of insurance.

⁹⁵ Heydon (n 94) [9.235], [9.240]. See also Mitchell (n 93) [1-08], [10.4]-[10.6], [10.30]-[10.38].

⁹⁶ Mitchell (n 93) [10.105], [10.106]; Heydon (n 94) [9.240], [9.285].

⁹⁷ S R Derham, *Subrogation in Insurance Law* (The Law Book Company Limited 1985), 17, 69, 72.

⁹⁸ *ibid* 69.

⁹⁹ *British Cash and Parcel Conveyors Limited v Lamson Store Service Company Limited* [1908] 1 KB 1006 (CA), 1012; *ibid* 104-5.

parties towards each other – are inapposite to application to the litigation funding context.

A defendant with liability insurance

Secondly, where a defendant has liability insurance, an insurer may take over conduct of the defence.¹⁰⁰ The extent of the insurer's authority and discretion to conduct proceedings turns on the terms of the policy.¹⁰¹ It is usual, however, for the insurer to be entitled to defend the claim, to appoint the solicitor, and to have discretion in the conduct of the defence; conversely, the insured will usually be under an obligation to cooperate with the insurer, and not to admit liability without the consent of the insurer.¹⁰² It has been said that the relationship entails that the solicitor has a retainer with the insurer, and also a retainer with the insured, but the terms of the policy may (and commonly do) provide for a joint retainer, or for the insured to relinquish control of the litigation and waive privilege in favour of the insurer.¹⁰³

The doctrine of subrogation will usually be inapplicable in these circumstances, because that doctrine applies only where the insurer has already fully indemnified the loss of the insured.¹⁰⁴

¹⁰⁰ The litigation will be carried on in the name of the insured party: *Murfin v Ashbridge* [1941] 1 All ER 231; Robert M Merkin and Raoul P Colinvaux, *Colinvaux & Merkin's Insurance Contract Law* (Sweet & Maxwell), B-0912.

¹⁰¹ Merkin, *Insurance Contract Law* (n 100) B-0911.

¹⁰² Tom Leech, 'Acting for the Insurer and the Insured: Dual Retainers and Conflict of Interest' (2008) 24 *Professional Negligence* 231, 232. See also John Birds, Ben Lynch and Simon Paul, *MacGillivray on Insurance Law* (14th edn, Sweet & Maxwell 2018), [30-068].

¹⁰³ *Brown v Guardian Royal Exchange Assurance Plc* [1994] 2 Lloyd's Rep 325 (CA), 330; *TSB Bank Plc v Robert Irving & Burns* [2000] 2 All ER 826, [11], [13]; Alison Padfield, 'Handling Professional Indemnity Coverage Issues in Cases of Suspected Fraud - Part II: Handling Conflicts of Interest between Insured and Insurer: The Lawyer's Dilemma' (12 September 2011) <http://www.devereuxchambers.co.uk/assets/docs/general/handling_conflicts_-_ap.pdf> accessed 10 October 2018, [5]-[10]; Robert Merkin, *Colinvaux's Law of Insurance*, vol 11 (Judith P Summer and Laura Hodgson eds, Sweet and Maxwell 2016), [21-081].

¹⁰⁴ Merkin, *Colinvaux's Law of Insurance* (n 103) [21-074].

The reason why third-party control is countenanced in the insurance context is because it is assumed that there is a common interest between the two parties in minimising any judgment awarded.¹⁰⁵ But this is not always the case.

The financial interest of the insured defendant depends on the quantum of the claim, relative to the limit of the insurance policy.

First, if the quantum exceeds the limit of the policy, then the insured defendant will have to pay the shortfall.¹⁰⁶ In these circumstances, the insured party therefore has a financial interest in the outcome, both in ensuring that the quantum of the claim remains within the limit of the policy, and also in ensuring that any shortfall is minimised. Conversely, if it is clear that the quantum of a claim will exceed the policy limit, then the interests of the insurer are quite different: if it is able to successfully defend the claim, then it will avoid liability, but if the claim is successful, the policy limit will place a cap on its exposure.¹⁰⁷ In those circumstances, the insured may wish to settle as close as possible to the policy limit, whereas the insurer has little incentive to take this course and may well prefer to defend the claim.¹⁰⁸ This situation has obvious ethical implications. The insurer will have conduct of the defence, but the insured remains the true party to the litigation, and also retains a financial interest in the outcome. There there is a clear potential for the interests of insured and insurer to conflict.¹⁰⁹

¹⁰⁵ *Groom v Crocker* [1939] 1 KB 194 (CA), 203 (Sir Wilfred Greene MR).

¹⁰⁶ Merkin, *Insurance Contract Law* (n 100) B-0913.

¹⁰⁷ *ibid.*

¹⁰⁸ *Distillers Co Bio-Chemicals (Aust) Pty Ltd v Ajax Insurance Co Ltd* (1974) 130 CLR 1, 23 (Stephen J); Merkin, *Colinvaux's Law of Insurance* (n 103) [21-079].

¹⁰⁹ *Distillers Co Bio-Chemicals* (n 108) 29.

Secondly, if the quantum is well within the limits of the policy, then the insured has no financial interest in the outcome.¹¹⁰ But there is still the possibility of conflict. The insurer might wish to settle against the wishes of the insured: for example, in a claim for professional negligence, a solicitor or doctor might deny their negligence, and wish to defend their position (which might have implications for their professional reputation).

It is nevertheless accepted that the prospect of conflict does *not* preclude the insurer from having conduct of the litigation, nor the solicitor from being jointly retained by both.¹¹¹ How, then, is insurer control to be reconciled with the possibility that the insurer and insured might have conflicting interests? It depends on the circumstances.

First, it is recognised that it is usual for the insurer to control litigation, and ‘may act predominantly in its own interest in doing so’.¹¹² Where the interests are aligned, it ‘may not be necessary to involve [the insured] closely in the decision-making’.¹¹³ An insurer may conduct the litigation as they see fit, ‘provided that they do so in what they bona fide consider to be the common interest of themselves and their assured’.¹¹⁴ Indeed, it has been recognised that allowing the insured defendant to ‘interfere with the conduct of proceedings’ by instructing the solicitors would defeat ‘the whole object and usefulness’ of provisions which confer control on the insured.¹¹⁵

¹¹⁰ Merkin, *Colinvaux's Law of Insurance* (n 103) [21-079].

¹¹¹ *Oceanic v HIH* [1999] NSWSC 292, [59].

¹¹² *Cormack & Anor v Washbourne* [2000] CLC 1039 (CA), 1048 Auld LJ (Nourse and Tuckey LJ agreeing).

¹¹³ *ibid.*

¹¹⁴ *Groom* (n 105) 203 (Sir Wilfred Greene MR). It has been suggested that this is an aspect of the obligation to act in utmost good faith: see Merkin, *Insurance Contract Law* (n 100) B-0914 – B-0917 as to the authorities on point, and the difficulties with this analysis.

¹¹⁵ *Groom* (n 105) 203 (Sir Wilfred Greene MR).

The requirement that the insurer act in the common interest means that they cannot act in accordance with ‘extraneous considerations’.¹¹⁶ So, for example, in the leading case of *Groom v Crocker*, it was impermissible for the solicitor, on the insurer’s instructions, to make admissions contrary to the interests of the insured, as part of a broader strategy by the insurer to settle several unrelated pieces of litigation with the claimant. This obligation in circumstances of conflict is expressed as applying both to the insurer and solicitor.¹¹⁷

Secondly, if a ‘significant’ conflict arises, then ‘the insurer should have regard both to its own interest and to the separate interest and exposure of the insured’.¹¹⁸ This might entail that the insured has greater involvement, but¹¹⁹

The manner and extent of such greater involvement of the insured are clearly matters of judgment and balance depending on the facts of each case.

In situations of conflict, the insurer must exercise their powers with ‘due regard for the interests of the insured’.¹²⁰

The solicitor will owe the insured defendant fiduciary duties, even if the insurer is providing instructions.¹²¹ However, if the insurer is entitled to appoint and instruct the solicitor, the duties of the solicitor to the insured defendant are *not* the same as if the defendant instructed the solicitor directly.¹²²

¹¹⁶ *ibid* 223 (Scott LJ).

¹¹⁷ *Nigel Watts Fashion Agencies Pty Ltd v GIO General Ltd* [1994] NSWCA 365 (per Kirby P and per Handley JA).

¹¹⁸ *Cormack* (n 112) 1048 Auld LJ (Nourse and Tuckey LJJ agreeing).

¹¹⁹ *ibid*.

¹²⁰ *Distillers Co Bio-Chemicals* (n 108) 29.

¹²¹ *Oceanic* (n 111) [39]; Charles Hollander and Simon Salzedo, *Conflicts of Interest* (Sweet & Maxwell 2016), [15-024]; *Birds* (n 102) [30-050].

¹²² *Groom* (n 105) 202-3 (Sir Wilfred Greene MR), 226-7 (Mackinnon LJ). See also *TSB Bank* (n 103).

Nevertheless, an important limit is placed on the freedom of the insurer to instruct the solicitors. The solicitor may *not* act on instructions of the insurer if those instructions would require that the solicitor ‘does something to which the insurers... are not entitled to require the assured to submit’, and will be in breach of their duties to the insured defendant if they do so.¹²³

But even in circumstances where the policy confers authority and full discretion on the insurer to take all the steps which the insured defendant would otherwise take, the Privy Council has recently held in *Ramsook v Crossley*¹²⁴ that the insurer does not have ‘carte blanche... to conduct proceedings in their own interests’ without regard to the insured’s denial of responsibility or the likelihood that the result would affect them (in the circumstances of that case, the judgment greatly exceeded the policy limit).¹²⁵ Even where the policy confers an unfettered authority and discretion, the solicitor (and the insurer) has a duty to ‘ascertain[] and consider[] [the insured’s] position, with a view to deciding whether it was appropriate simply to admit liability on [the insured’s] behalf’, and to keep the insured informed.¹²⁶ In respect of the conflict which arises where the liability is greater than the limit of the policy, prior to *Ramsook v Crossley*, it had been suggested that one route available to the solicitor would be for the insured and insurer to agree that each should take separate advice on the specific question of settlement.¹²⁷

¹²³ *Groom* (n 105) 203 (Sir Wilfred Greene MR). See also *TSB Bank* (n 103).

¹²⁴ *Ramsook v Crossley (Trinidad and Tobago)* [2018] UKPC 9.

¹²⁵ *ibid* [27] (Lord Mance, delivering the judgment of the Board). As to the duty to bring risks to the attention of the insured, see also *Nigel Watts Fashion Agencies* (n 117) (per Kirby P)

¹²⁶ *Ramsook* (n 124) [27] (Lord Mance, delivering the judgment of the Board).

¹²⁷ *Hollander* (n 127) [15-025].

The solicitor must take into account the interests of the insured, and notify the insured if there is a conflict.¹²⁸ If the insured gives instructions that the insurer will not agree to, then the insurer may cease to conduct the proceedings. If the insured gives instructions which it is *not* entitled to give, then those costs may not be recoverable under the policy.¹²⁹

A further point of conflict may arise where a solicitor becomes aware, in the course of proceedings, of facts which would entitle the insurer to deny cover under the terms of the policy. In those circumstances, it has been suggested that the solicitor will be obliged to inform both the insured and insurer immediately, in order to avoid a breach of their fiduciary duties.¹³⁰

Statutory regulation

In addition to the court-developed principles identified above, there are certain statutory provisions which affect the position of a solicitor who acts in respect of insurance matters.

In Australia, the *Insurance Contracts Act 1984*¹³¹ relevantly provides that each of the parties is under an implied duty of utmost good faith towards the other.¹³² It also provides that, before entry into the insurance contract, the insured has a duty to disclose to the insurer every matter which they know to be relevant to the insurer's decision to

¹²⁸ Merkin, *Colinvaux's Law of Insurance* (n 103) [21-081].

¹²⁹ *Groom* (n 105) 227-8 (Mackinnon LJ). See also *TSB Bank* (n 103). As to the obligation to bring conflicts to the attention of the insured, see also *Nigel Watts Fashion Agencies* (n 117) (per Kirby P).

¹³⁰ *Hollander* (n 127) [15-024]. The facts in *TSB Bank* (n 103) provide a particularly stark example of a solicitor's failure to act in accordance with this suggestion, although the Court of Appeal limited its analysis to the question of privilege, and did not consider the issue of the solicitor's duties, to avoid pre-empting any potential disciplinary proceedings.

¹³¹ Insurance Contracts Act 1984 (Cth).

¹³² *ibid* s 13(1).

insure, as well as matters which a reasonable person could be expected to know to be relevant.¹³³ The Act provides for the consequences of non-disclosure.¹³⁴

Clearly, neither of these provisions directly bears upon a solicitor's professional obligations. But in both cases, the existence of such a provision could pre-empt some of the conflict issues that might arise. For example, if the insured complies with their duty of disclosure, then the solicitor is correspondingly less likely to encounter a conflict in the form of becoming aware, during proceedings, of matters which would entitle the insurer to avoid liability under the insurance contract.

The utility of a comparison with insurance

Several commentators have argued that the conflicts of interest which arise in the funding context are similar to those which arise in the insurance context. Accordingly, they suggest that ethical dilemmas in litigation funding are overstated: they can be resolved by applying principles of law which have been developed in the context of insurance.

Two principal exponents of this view are Sebok and Wayne. Each suggests that the law concerning the conduct of litigation by an insurer on behalf of an insured defendant demonstrates that litigation may be controlled by a person who is not a party.¹³⁵ Wendel¹³⁶ and Silver¹³⁷ each identify that there are risks inherent in the fact that there are three parties involved in funded litigation – funder, lawyer and claimant – whose interests may diverge at points in the litigation process. Each draws an analogy

¹³³ *ibid* s 21(1).

¹³⁴ *ibid* s 28.

¹³⁵ See, eg, Wendel (n 18) 140-51; Walker (n 11) 107-8.

¹³⁶ Wendel (n 18) 140-51.

¹³⁷ Silver (n 17) 628-30.

with the position of an insurer in this respect, and observes that insurance law has developed principles to regulate the possibility of conflict. Walker also suggests that any conflicts might be reconciled through requiring that a lawyer prioritise the duty to and interests of the claimant over that of the funder, noting that insurance law has developed principles for regulating the relationship between insurer and insured which might be applied by analogy.¹³⁸

The critical difficulty in such an argument is that the insurer's entitlement to control litigation – which is provided for expressly in the terms of the insurance contract – is tempered by an obligation to take into account the insured's best interests, and the obligation of utmost good faith. In the funding context, there is no such obligation.

Further, the insurance situation is different in a critical respect. In most cases, the insurer has the only financial interest. Even where the quantum is reached, the insurer will have the primary financial interest. It is therefore unsurprising that the law has been prepared to countenance the idea that the insurer may have primary control over (1) whether to litigate about liability or quantum and (2) how much the insurer will provide by way of settlement.

Conversely, in the funding situation, the claimant will always have a financial interest in the outcome, and usually this will be the primary financial interest. The case for permitting a funder to act in its own interests is therefore less weighty.

There are clear principles in the insurance context about how to reconcile the interests of the insurer and the insured, because courts and market participants have grasped the nettle of providing for complete control of litigation by an insurer, in clear and unambiguous terms. Insurance law principles do not presently assist in resolving

¹³⁸

Walker (n 11) 107-8.

issues in litigation funding, because they do not apply. Moreover, it is not entirely clear that they ought to – in England, because funder control is not countenanced in the same way as insurer control, and in both jurisdictions because there is in any event a diversity of market practices.

What can be drawn from the insurance context?

Nevertheless, there are several points that may be drawn from the relevant law which are applicable across to funding.

First, insurance law indicates that a solicitor's professional ethics can accommodate *potential* conflicts, and also provide guidelines for the point at which a potential conflict is transformed into an actual conflict which requires the solicitor to take action.

Secondly, insurance law provides a clear set of guidelines as to what a solicitor ought to do when an actual conflict arises.

Thirdly, insurance law demonstrates the importance of the terms of the contract between insurer and insured as to the level of control which the insurer is permitted to exert. As set out above, in many cases the insured's rights and/or the solicitor's obligations are contingent upon those terms. Transferred across to the funding context, this indicates that the funding agreement may be critical to (1) the level of control which the funder can permissibly exert and (2) a solicitor's obligations may well be contingent on the terms of that agreement.

Finally, the insurance context indicates that even where a third party has an unfettered right to control litigation, this cannot enable the third party – or, importantly, the solicitor – to overlook the client's interests. If this is true in the insurance context,

where the insurer may well have the sole financial interest in the litigation, it is *a fortiori* in the litigation funding context, where the funder has only a percentage interest.

This thesis has adopted the view that there is no reason to eschew funder control, provided that it is clearly agreed and the interests of the funded claimant are properly protected. To the extent that the concept of funder control is fully embraced, insurance law principles provide an indication of how these interests may be protected.

What should be done?

Application of specific ethical rules

As explained above, some of the ethical questions which are raised concern the applicability (or otherwise) of specific rules to the litigation funding context. For example, is there a duty to inform claimants about litigation funding? These specific rules can – and should be – addressed simply by amendments which clarify whether or not litigation funding falls within the rule.

Entry into the funding agreement

There are three issues at the point of entry into the funding agreement: who does the solicitor act for? What is the content of the funding agreement? What disclosure ought to be made to the claimant?

Who does the solicitor act for?

As a starting point, it needs to be clear who the solicitor acts for at the time that the funding agreement is entered into. For sophisticated claimants, it probably does not matter who the solicitor acts for, provided all parties know who is the client. For example, an insolvency practitioner with experience in funding might be able to

negotiate the terms of a funding agreement without the assistance of a solicitor, or with the assistance of a solicitor who provides them with day-to-day advice (rather than the solicitor who will conduct the litigation).

In the context of class actions, the solicitor who conducts the proceedings ought to give advice to the claimants about the content of the funding agreement. It would be inefficient and expensive for each individual class member to seek independent advice. In order to ensure that full information is provided, having regard to the difficulty in advising many claimants, it would be beneficial to have some prescription about what information is given to claimants. This could avoid allegations that solicitors and/or funders have failed to disclose important terms to their clients.¹³⁹

Similarly, impecunious claimants ought to receive advice on the funding agreement from the solicitor who conducts proceedings. Requiring independent advice from another solicitor would impose costs which, ex hypothesi, the impecunious claimant will not be able to afford.

The ALF Code provides that there is an obligation on the funder to ensure that the claimant receives independent legal advice upon entry into the funding agreement. Given the history of the ALF Code, and the absence of any other regulation, the purpose of this provision is readily understandable. But the content of solicitor's obligations ought to be included in rules which are directed towards and are binding on solicitors.

The solicitor's role in advising on the funding agreement

It is clear that some of the ethical problems which solicitors might face during the course of funded litigation could be circumvented by careful drafting of the funding

¹³⁹ As in David Marin-Guzman, 'Class Action Funding Deal over Casuals Referred to ACCC' *Australian Financial Review* (11 October 2018) <<https://www.afr.com/news/policy/industrial-relations/class-action-funding-deal-over-casuals-referred-to-acc-20181011-h16iy7>>.

agreement. Questions such as the identity of the client, and the extent of any obligations to the funder, can and should be dealt with at the stage of entry into the funding agreement. The problem of who decides critical matters in the litigation – such as tactical decisions in the proceedings, and decisions about settlement – may be pre-empted and mitigated by ensuring that this is dealt with exhaustively in the funding agreement, and that the claimant has had independent advice on this topic, and understands the implications of the terms.

If these issues are dealt with and properly understood then, later problems may be pre-empted. By comparison, in the insurance context, issues regarding the extent of the control which the insurer may permissibly exert are contingent on the terms of the policy.

There are two issues, therefore. First, the funding agreement must actually contain provisions dealing with these critical matters. This raises the question of required terms of funding agreements. Secondly, the claimant must understand the significance of provisions in the funding agreement. This raises issues of disclosure.

Required terms of funding agreements and/or retainers

As a minimum, the retainer and/or the funding agreement (as appropriate) ought to deal with the following matters:

- Who is the solicitor's client? Is it just the claimant, or is there a joint retainer with the funder?
- What are the duties and/or obligations of the solicitor towards the funder?
- What, precisely, are the arrangements for taking instructions, and for communicating information, to each of the claimant and the funder?
- What level of control is contemplated?

- What information must be communicated to the funder? For example, is the funder entitled to be informed about all matters which are relevant to the progress of the cause of action? A provision dealing with this subject might pre-empt questions about privilege, but also pre-empt questions about whether a solicitor can inform the funder about facts which come to light during litigation which adversely affect the prospects of the claim.
- A dispute resolution procedure – this is addressed separately below.

Disclosure to claimant

In order to ensure that the claimant fully understands the implications of the funding agreement, there ought to be an ethical obligation on solicitors to explain fully the implications of a litigation funding agreement. There is presently a disclosure obligation in the SRA Handbook concerning conditional fee arrangements, so this sort of ethical obligation is not novel.

Disclosure by the claimant

In the insurance context, the insured is required to disclose certain matters to the insurer prior to entry into the insurance policy. Introducing a similar obligation on a funded claimant could pre-empt later difficulties, by reducing the prospect that a solicitor might be put in a position where they come across information which might entitle the funder to terminate the funding agreement. In the class action context, the ALRC has recommended that the Federal Court practice note ought to require solicitors to identify, in the first notice to class members, the obligations of lawyers and funders to avoid any conflicts which arise, and the details of any conflicts in the case.¹⁴⁰ There is merit in

¹⁴⁰ Australian Law Reform Commission, *Integrity, Fairness and Efficiency* (n 3) [7.162]-[7.177].

expanding this to all class actions, and indeed beyond the class action context to all funded proceedings.

Control of litigation and disputes

This thesis has suggested that there is little reason to restrict a funder's ability to control litigation. Nevertheless, it is critical that the funder and claimant agree about the extent of funder control and that the claimant's position is properly protected. Disputes about the level of control ought to be mitigated by full disclosure to the claimant at the time of entry into the funding agreement about what is envisaged, as well as fulsome treatment in the funding agreement.

There is still a risk that despite the terms of a funding agreement, a funder may seek to exert commercial pressure on a solicitor to cede to it a greater degree of control. Part of the difficulty with the current state of regulation (including court judgments) is that it appears that there is a level of input and/or influence which is acceptable, but which falls short of 'control'. Further, in England, there is a question about whether a funder who provides input into the litigation process is providing instructions – and therefore contravening the rules about taking instructions only from one's client. It would be helpful to the proper discharge of solicitors' ethical obligations if regulatory guidance were provided which articulated in clear and specific terms what is to be treated as impermissible 'control'.

One possible solution is to have a rule to the effect that where parties disagree about the conduct of the litigation, the claimant's views must prevail. The difficulty with this is that it would not avoid the situation in *Excalibur*, where the claimant persisted in a course of conduct which was heavily criticised by the court. Another alternative would be to adopt the solution from the insurance context: that the solicitor

and funder cannot force the claimant to do anything that the claimant could not be compelled to do by the terms of the funding agreement. This is, however, not a sufficiently broad rule, and would not address the possibility of a funder exerting commercial pressure on a solicitor.

The most prospective solution is likely to be a dispute resolution procedure along the lines currently imposed by the ALF – that is, resolution by the opinion of a senior counsel briefed by either both funder and claimant jointly, or appointed by the chairman of the Bar Council.¹⁴¹ Ideally, the funding agreement would also be required to prescribe the timeframe for obtaining such an opinion, to avoid the risk that the dispute resolution process would jeopardise the progress of the litigation.

There is, of course, a theoretical risk that frequent resort to a dispute resolution procedure could slow down the litigation process. In practice, however, if this were to happen repeatedly, it would likely diminish the value of the claim, because it would increase the risk of the court exercising its case management powers to strike out the claim. A diminution in the value of a claim would likely trigger the funder's entitlement to terminate the funding agreement.

Importing rules from the insurance context

Insurance law principles have been developed on the premise that the insurer will control litigation. The extent to which insurance law principles are apposite to the funding situation is therefore contingent on the extent to which funding agreements entail funder control – and, in circumstances where the funder does control litigation, insurance law principles provide a good source of rules as to how the interests of the

¹⁴¹ ALF, *Code of Conduct* (n 38) [13.2].

claimant may be protected. However, as explained earlier, there is a diversity of practice in both jurisdictions, and the law in England does not presently encourage funder control.

A solicitor having a financial interest in a funder

As set out above, there is authority in Australia to indicate that in some circumstances a solicitor or barrister will be precluded from having a financial interest in a funder. However, it is unclear what the dividing line is. In the interests of clarity for solicitors, and in the interests of maintaining the appearance of integrity of the profession, there ought to be clear guidance concerning the circumstances (if any) in which a solicitor or firm may have an interest in a funder which is funding litigation in which the solicitor or firm is acting, and the extent of the permissible interest.

There are clear reasons for prohibiting the practice all together.¹⁴² First, as explained in the previous chapter, there are various points in litigation where funder and claimant may have differing interests; if the solicitor had an interest in the funder, this would lead to a conflict of interest for the solicitor. It would seem to preclude the application of insurance law principles, if that is adopted as a route for resolving existing ethical dilemmas. Secondly, this thesis has suggested that the separation between funder and solicitor has the potential to confer benefits, such as independent scrutiny of solicitor's fees. If the funder and solicitor are too closely related – such as where one has a financial interest in the other – these sorts of benefits will be lost.

¹⁴² This was one of the ALRC's recommendations: Australian Law Reform Commission, *Integrity, Fairness and Efficiency* (n 3) [7.149]-[7.161].

Actual conflicts

It is suggested that the problem of actual conflicts of interest, when they arise, is perhaps the easiest. The advantage of the fact that rules of legal professional ethics are non-specific – and are generally expressed as principles which ought to inform the claimant – is that they can adapt to fresh situations.

Provided that the status of the funder is clear – i.e. whether they are a client or not, and/or whether any other duties are owed to them – then situations of actual conflict ought to be capable of resolution in accordance with usual rules of professional conduct, and/or the dispute resolution provisions in the funding agreement.¹⁴³

Conclusion

This chapter commenced by considering some commercial forces which affected the solicitor-funder relationship, and also the nature of the conflicts which might arise in the course of funded litigation, and the duties and interests which the solicitor has at critical points.

Gaps and limitations in the existing regulation of solicitors' ethical obligations were then addressed. In some cases, it is not clear how general rules concerning solicitors' obligations are applicable in the funding context, and in other cases it is not clear whether specific rules are intended to cover litigation funding. It was then argued that further regulation was likely to be needed, both in the interests of clarity, and also because current market forces – which seemed to favour scrupulous behaviour – might not continue in the future, or be present in all parts of the litigation funding industry.

¹⁴³ Cf Wendel (n 18) 149-50.

The chapter concluded by considering options for regulation. First, the position of solicitors acting for insurers was compared and contrasted, and some guidance was drawn from this. The chapter then identified particular areas where further regulation of solicitors' professional obligations would be desirable, and some options for reform, including specifically:

- Amending existing solicitor's rules of practice, and rules of court, to make clear whether litigation funding is included in existing obligations (insofar as there is presently ambiguity or uncertainty).
- Identifying prescriptively the information which ought to be given to class claimants concerning the terms of the funding agreement.
- Prohibiting solicitors and firms from having any financial interest in an entity which is funding litigation in which the solicitor or firm is retained.
- If it is accepted that funders may exert control over litigation in the same manner as an insurer, then insurance law principles concerning the protection of the claimant's interests ought to be adopted for the funding context.

CHAPTER 12: CONCLUSION

It is trite to observe that there are many barriers to those who would seek to access the courts: these include the complexity of the litigation process; the high and unpredictable cost of litigation; and the potential for disproportionality between the value of a claim and the cost of litigating it. These barriers affect poor and well-resourced alike.

Litigation funding is a market response to these barriers to justice. It is one amongst a variety of market and regulatory responses – none of which is a panacea for the seemingly intractable challenge of providing access to justice to an appropriate level and at an acceptable cost to the public purse.

Litigation funding is a practice which, for centuries, would have been impermissible as involving champerty. It also entails the commodification of legal claims, in the context of the legal profession having eschewed market rhetoric for centuries. Accordingly, it is unsurprising that the emergence of the litigation funding industry was greeted with some circumspection. As this thesis has explained, judicial acceptance of litigation funding was largely driven by pragmatic concerns about access to justice, rather than by any sense that these historical concerns were misplaced or outdated.

This thesis has examined the place of litigation funding in the civil justice system, a task which had not previously been squarely addressed.

We have seen that the emergence of litigation funding is consonant with broader developments in civil justice. The Woolf reforms in England, and their counterparts in Australia, represent a deliberate choice of a proportionate approach to litigation, at the expense of party autonomy. Policymakers have also chosen to privatise the cost of

litigation, and to introduce to the legal profession market values which had for centuries been rejected in its own self-regulation. Litigation funding is an unsurprising feature of this landscape.

Residual reticence about the third-party commercial funding of litigation can, in part, be explained as a vestige of an earlier age of civil justice, in which party autonomy was sacrosanct, and the legal profession eschewed market rhetoric. For better or worse, that age is now past.

It can also be explained, in part, by the sometimes-confused attitudes of policymakers, and participants in the civil justice system, towards the value of litigation. On one hand, the past fifty years has seen a great increase in the creation of new laws, the recognition of human rights (including the right of access to justice, necessary for the enjoyment of all other rights), an increase in ‘juristocracy’, and the introduction of devices such as class actions which are intended to facilitate access to court. These trends indicate that litigation is desirable as a process for resolving disputes and protecting rights. On the other hand, litigation is discouraged by rules of court which strongly encourage settlement, by the imposition of court fees, and by the emergence of various forms of alternative dispute resolution. Some commentators suggest that litigation is economically deleterious in diverting the attention of litigants away from more productive activities.

The desirability of litigation funding is obviously connected with perceptions about the claim being funded (including whether it is meritorious), and about the use of litigation more generally. Because the value of litigation itself is, to some extent, contested, it is perhaps unsurprising that the value of litigation funding is also contested.

The rapid emergence of litigation funding, and its somewhat unsettled position in the civil justice system, has affected its regulation. At present, the regulation of litigation funding is in an unsatisfactory state, largely consisting of voluntary self-regulation and court-developed rules. It has developed in a manner which has been piecemeal and reactive. Too often, suggestions about how funding might be regulated have been driven by concerns about one part of the market – often, class actions – or by concerns about the value of litigation more generally.

But once it is recognised that litigation funding is a consistent part of the modern landscape of civil justice, then it is possible to grapple with regulatory issues more comprehensively. This thesis has sought to identify some of the market failures which may exist or arise in the litigation funding market (and the extent to which those might now be occurring in practice), and has made some broad suggestions for how they might be regulated.

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