LSLA
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Date	11 May 2018
Publication	New Law Journal
Type of publication	Legal

New Law Journal
Leading on debate, litigation and dispute resolution

A costs conundrum

Can litigation funding negate a security for costs application, asks Georgina Squire

IN BRIEF

- Litigation funding is on the rise and greater scrutiny from the courts has followed.
- Funders have looked to the support of after the event insurance policies, but these have also been put under the microscope.
- The 'Arkin Cap' is now a significant consideration for third party funders when assessing whether and at what level to provide funding for litigation.

We are all seeing a rise in litigation funding, evidenced recently by the explosion in profits of one significant AIM listed funder, Burford Capital LLC. Burford's 2017 Annual Report shows income up by 109% to £341m and profit after tax up by 130% to £265m.

However, with this rise in funding, comes greater scrutiny by the courts of the role of funders in litigation and their potential liability to other parties. Recent case law has increased that potential liability. Funders often look to the support of an after the event (ATE) insurance policy to lay off some of their own risk. Again, the weight that can be given to the value of an ATE insurance policy has been under renewed scrutiny of the court recently.

Background

By way of background, the Court of Appeal decision in *Arkin v Borchard Lines and Others* [2005] 1 WLR 3055, [2005] 3 All ER 613 concerned a third party funder's liability to pay a defendant's costs when an impecunious claimant had received an adverse cost order. The defendants applied for orders for costs against the third party funder under s 51of the Supreme Court Act 1981. At first instance, the judge dismissed the application.

On appeal this was overturned, the court giving weight to the general rule in CPR r 44.3 (that a successful party should recover his costs) and deciding that the third party funder should be liable for costs of the opposing party to the extent of the funding that was provided. This became known as the 'Arkin Cap'. It is now a significant consideration for third party funders when assessing whether and at what level to provide funding for litigation.

In the recent 2017 case of *Sandra Bailey and Others v GlaxoSmithKline UK Limited* [2017] EWHC 3195 (QB), [2018] 4 WLR 7 the defendant applied for security for costs from the claimants' litigation funder. Mr Justice Foskett noted that the decision in *Arkin* had alluded to removing the 'Arkin Cap' if it was inappropriate. He decided that the third party funders should pay half of the figure for security of costs that he had arrived at. One third of the value of the ATE insurance policy was also applied as security for a further proportion of the costs—the deduction reflecting the risk that the policy may be avoided at some stage. This decision allowed the claimants to rely upon the ATE insurance policy for a proportion of the security for some of the estimated costs, but their third party funders were exposed directly to an order to put up security, too.

Key decisions

There have been several key decisions in recent years on the availability of ATE insurance policies to satisfy an application for security for costs. The *Sandra Bailey* case is one of the more recent decisions. An even narrower approach when determining the level of security for costs which could be provided by an ATE insurance policy was applied in *Premier Motorauctions Ltd (in Liquidation) and Another v PriceWaterhouseCoopers LLP and Another* [2017] EWCA Civ 1872, [2018] Lloyd's Rep IR 123. The claimants obtained ATE insurance from multiple insurers. At first instance, the judge held that the ATE insurance policies were together sufficient security for costs. On appeal, this decision was overturned. It was held that the ATE insurance policies were not adequate for security for costs as there was no guarantee that the claimants' actions would not invalidate the policy and see them avoided.

Conundrum

Insurance policies are contracts between insurer and insured. As there is therefore no automatic control which can be exercised by any external third party over whether an insurer will decline to pay under an insurance policy due to alleged breaches of conditions or obligations by the insured, the opponent will no doubt recognise, as did the court in *Premier Motorauctions*, that there is uncertainty as to how much any third party can rely on the existence of an ATE policy. It is a conundrum, as claimants without the means to fund litigation are those most exposed to security for costs applications. They are the very same parties who would want to look to their ATE policy or third party funder to help support their adverse costs risk. Sometimes they may achieve such support, but it can come at an enhanced cost to the claimant. Unless the ATE insurance policy has non-avoidance clauses or the insurer provides some sort of additional assurance which can be relied on by the defendant, it seems the policy may well not be adequate for security for costs.

This is particularly relevant when claims are brought on behalf of insolvent companies as their opponents are potentially exposed to costs risks and, unless a funder can step in and support them or an ATE policy is accepted as having sufficient weight to do so, adverse costs on an application for security for costs can have the effect of depriving of the ability to pursue a claim. This is a windfall benefit for a defendant, but a disastrous situation for an impecunious claimant. It seems a harsh situation—but one reflected by recent authorities. NLJ

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