Article

Non-party cost orders: an inevitable consequence of funding litigation?

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As has been widely reported, the litigation funding landscape in the Cayman Islands is changing to keep pace with the UK, Australia and other common law jurisdictions.[1] The Caymanian judiciary acknowledge that provided adequate protections are in place, a funding arrangement can facilitate better access to justice and the Legislative Assembly is in the process of enacting legislation to reflect that position. Whereas formerly claims with merit may not have been able to be pursued in Cayman due to a lack of funding, the potential to access third party funding is likely to lead to the rapid development of a sophisticated funding environment.

Funding a claim as a third party carries the potential to be made liable for the opponents' costs by way of a non-party costs order ("NPCO"). It is important that funders and their advisors consider how best to protect themselves from any exposure to a NPCO, as the use of external funding increases in Cayman.

General principles

The applicable principles, taken from a line of cases from 1993 onwards, were summarised by the Privy Council in *Dymocks Franchise Systems (NSW) Pty Ltd v Todd and others (No.2) [2004] 1 WLR 2807*.

Is it just to make an order?

Although costs orders against non-parties are described as "exceptional", this means no more than the case is outside the normal run of cases whereby parties pursue or defend claims for their own benefit and at their own expense. The ultimate question in any such "exceptional" case is whether, in all the circumstances, it is just to make the order.

Does the non-party have an interest in the outcome and exert any control?

As a rule, the court's discretion will not be exercised against "pure funders", described in the case law as those with no personal interest in the litigation, who do not stand to benefit from it, are not funding it as a matter of business and in no way seek to control its course.

Where the non-party funds, controls and benefits from the proceedings, justice will ordinarily require that, if the proceedings fail, the non-party will pay the successful party's costs. The non-party in such a case is not so much facilitating access to justice as they are taking advantage of it for their own purposes. In such a case, the funder is considered to be a "real party" to the litigation.

[1] Conyers' recent articles on litigation funding:
https://www.conyers.com/publications/view/application-granted-for-sanction-to-enter-into-a-litigation-funding-agreement/

https://www.conyers.com/publications/view/a-company-v-a-funder-unreported-23-november-2017/

https://www.conyers.com/publications/view/the-cayman-islands-welcomes-third-party-litigation-funders/

Generally speaking, where a non-party promotes and funds proceedings brought by an insolvent company solely or substantially for their own financial benefit, they are likely to be liable for the costs if that claim fails. However, there are exceptions. For example, where the non-party is a director or court-appointed liquidator who can realistically be regarded as acting in the interests of the company (and more especially its shareholders and creditors), rather than in their own interests, that non-party is unlikely to be penalised with a NPCO.

Limitations on NPCOs: causation and the Arkin cap

The English Court of Appeal has stated that, although not a precondition, it is usually "a vital factor" that the non-party caused the costs sought to be recovered (*Jobanputra and another v Modi and another [2014] EWCA Civ 1046*). Where a non-party funds litigation for a limited time or in respect of part of the relevant proceedings, the award may be limited to costs incurred during that specific period (see *Hamilton v Al Fayed [2002] EWCA Civ 665*).

In *Excalibur Ventures LLC v Texas Keystone Inc (No.2) [2014] EWHC 3436 (Comm)*, the court rejected an argument that funders who only came into proceedings halfway through should be liable for the costs of the action as a whole as, it was argued, the funders were trying to benefit from the work undertaken prior to the time that they started funding (by obtaining a share of the proceeds of the action if it were successful). This approach was endorsed and followed more recently in *Davey v Money [2019] EWHC 997 (Ch)*.

In *Burnden Holdings (UK) Ltd and another v Fielding and another [2019] EWHC 2995 (Ch)* the court made an NPCO against a firm which had funded unsuccessful proceedings brought by one of its partners as liquidator of a company. The NPCO was limited to the time period during which the firm provided funding. The funding ensured that the proceedings remained in existence and could therefore continue, but the judge did not accept that a "but for" test of factual causation was sufficient to fix a non-party funder with total liability.

In *Arkin v Borchard Lines Ltd and others [2005] EWCA Civ 665*, it was held that a professional funder who financed part of the costs of litigation should be liable for the other side's costs to the same extent as it had funded the costs of the losing litigant. This is often referred to as the "*Arkin* cap".

The "*Arkin* cap" has not been abolished but is no longer absolute. In *Davey v Money*, the court declined to apply the cap to a NPCO made against commercial funders. The funding was GBP 1.2 million but the costs ordered to be paid were GBP 3.9 million. The judge emphasised that the imposition of a NPCO was a matter of discretion, to be exercised based on what was just in the circumstances of each case. This meant that, on an application for non-party costs against a commercial funder, the court retained a broad discretion to decide the extent to which the funder should be liable for adverse costs. That liability will not necessarily be limited to the amount the funder has provided to fund the claim. It was noted that the *Arkin* cap was best understood as an approach that should be considered in cases involving a commercial funder as a means of achieving a just result in all the circumstances, not a rule to be applied automatically. For example, how the funder and the funded litigant have agreed to share in the proceeds of sale may be a relevant factor regarding the extent of the funder's liability.

In *Davey v Money*, the funder came on board after discovery and exchange of witness statements so had every opportunity to investigate and assess the types of allegations it was choosing to fund. The court held that the funder must have known that the costs were more than the amount they were willing to invest and that the plaintiff was unlikely to be able to pay them.

What does this mean for litigation funders in Cayman?

The litigation funding business is still developing in Cayman. In *A Company -v- A Funder (unreported, 23 November 2017),* it was held that, as a matter of principle, a funding agreement will not be unlawful by reason of maintenance and champerty if it does not have a tendency to corrupt public justice.

Whether or not an agreement had such a tendency would depend on a number of features, including:

- The extent to which the funder controls the litigation;
- The ability of the funder to terminate the funding agreement at will or without reasonable cause;
- The level of communication between the funded party and the solicitor;
- The prejudice likely to be suffered by a defendant if the claim fails;
- The extent to which the funded party is provided with information about, and is able to make informed decisions concerning the litigation;
- The amount of profit that the funder stands to make; and
- Whether or not the funder is a professional funder and is regulated.

Even if funders are able to satisfy key requirements, it is important that they heed the warnings in recent case law to minimise the risk of any exposure to a NPCO. Given that a funder chooses which claims to invest in, it cannot dissociate itself from the conduct of those it funds. Accordingly, if the losing funded party is found liable for costs on an indemnity basis, the funder is often required to contribute to those costs on the same basis.

The English Court of Appeal confirmed in *Excalibur Ventures LLC v Texas Keystone Inc and others [2016] EWCA Civ 1144* that:

- to minimise the risk of orders for indemnity costs against the funded party, funders should carry out extensive due diligence involving "rigorous analysis of law, facts and witnesses, consideration of proportionality and review at appropriate intervals". In addition, an on-going review by independent lawyers will often be essential. This will not render the funding agreement champertous; and

- a costs order can be made against a person who has provided funding and who, in reality, will receive the benefit of the litigation, even if they are not a party to the funding agreement (e.g. in *Excalibur*, the funder's parent company).

In the usual way, funders should form their own view on the merits of a claim and consider requiring after-the-event insurance be obtained to cover the risk of adverse costs. As for exerting control over the case, funders will want to ensure that, whilst they are kept up to date, they are not "intermeddling" and influencing decisions made in the litigation. The ability to utilise litigation funding in the Cayman Islands may be relatively new but there is a mature body of case law concerning litigation funding and NPCOs that funders can use to guide them.

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