A FUNDED CLAIM: THE DEFENDANT'S PERSPECTIVE

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A. Proceedings are Commenced

(i) Application for Security for Costs?

1. One of the first questions for the defendant to a professional negligence claim to grapple with when proceedings have been issued is whether or not to seek from the claimant security for the defendant's costs of fighting the action.

2. The jurisdiction is now to be found at CPR r.25.12 and 25.13 and the general principles relating to security are now fairly well established and are to be found most recently stated in two Court of Appeal decisions: *Jirehouse Capital v Beller* [2009] 1 WLR 751 and *SARPD Oil v Addax Energy* [2016] EWCA Civ 120. In essence:

   2.1 The court may make an order for security for costs if two conditions are satisfied (CPR r.25.13(1)):

   > (a) it is satisfied, having regard to all the circumstances of the case, that it is just to make such an order; and
   >
   > (b) (i) one or more of the conditions in paragraph (2) applies…

   2.2 Although there are a number of "conditions" on which the defendant applicant may rely to seek security the most frequently relied-upon condition is to be found at 25.13(2)(c):.[1]

   > "the claimant is a company or other body (whether incorporated inside or outside Great Britain) and there is reason to believe that it will be unable to pay the defendant's costs if ordered to do so"

[1] The other conditions are: "(2)….
(a) the claimant is:-
(i) resident out of the jurisdiction; but
(ii) not resident in a Brussels Contracting State, a State bound by the Lugano Convention, a State bound by the 2005 Hague Convention or a Regulation State, as defined in section 1(3) of the Civil Jurisdiction and Judgments Act 1982;
…
(d) the claimant has changed his address since the claim was commenced with a view to evading the consequences of the litigation;
(e) the claimant failed to give his address in the claim form, or gave an incorrect address in that form;
(f) the claimant is acting as a nominal claimant, other than as a representative claimant under Part 19, and there is reason to believe that he will be unable to pay the defendant's costs if ordered to do so;
(g) the claimant has taken steps in relation to his assets that would make it difficult to enforce an order for costs against him."

2.3 It was held in *Jirehouse* that the phrase "reason to believe" did not require the Court to conclude at the time of the application that it was "more likely than not" that the claimant would not be able to pay the defendant's costs if ordered to do so[2] (i.e. at a future point in time, being some time after the trial of the claim).[3] But the burden is upon the defendant to show the relevant "reason to believe."

2.4 In *SARPD* this condition was further glossed as follows, at [13]-[14]: "It follows that it is not sufficient for the court or the defendant to be left in doubt about a claimant's ability to pay the defendant's costs if the claimant loses. Nor is it sufficient as the first instance judge in *Jirehouse* had done to paraphrase the wording of the rule by saying that there was a significant danger that the claimants would not be able to pay such costs. The court must simply have reason to believe that the claimant will not be able to pay them….That is, as Arden LJ said, a matter of evaluation."

2.5 If a claimant declines to say anything about its financial position, there are no identifiable assets, and there are no publicly available accounts then security will usually be granted: *SARPD* at [17] and *Coral Reef Ltd v Silverbond Enterprises Ltd* [2016] EWHC 874 (Ch).

2.6 Although security will generally not be ordered where to do so would "stifle" a genuine claim, the claimant would have to show that it had no available means to put up as security, which extends to those interested in the claimant's claim: e.g. its shareholders, directors and backers.[4] The burden in showing this is on the claimant.

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[2] Per Arden LJ, at [26], [29]: "in my judgment, there is a critical difference between a conclusion that there is "reason to believe" that the company will not be able to pay costs ordered against it and a conclusion that it has been proved that the company will not be able to pay costs ordered against it. In the former case, there is no need to reach a final conclusion as to what will probably happen. In the latter case, a conclusion has to be reached on the balance of probabilities….I do not accept the argument … that the test of "reason to believe" must be elevated to a test of balance of probabilities simply because the matter to which the test relates is something which, as Sir Donald Nicholls V-C held, must be established and not simply identified as a possibility. That which has to be established is something that will occur only after the order for security is made. It can therefore only be a matter of evaluation. A person can have a reason to believe that a future event will occur."

[3] I.e. at a time when there has been judgment and an order for payment of account of costs has been made: see the approach take in *Dunn Motor Traction Ltd v National Express Ltd* [2017] EWHC 228 (Comm). The relevant date is not solely the date when the detailed assessment of costs will, hypothetically, have taken place.

[4] The principles were stated in *William Newman v Wenden Properties Ltd* [2007] EWHC 336 (TCC), by HHJ Coulson QC: "It is often argued that the application for security for costs, if allowed, would stifle a genuine claim. In consequence, the courts have refined this element of the discretion under CPR Part 25. It seems to me that the following principles are relevant to the present application: (a) Where an order for security for costs against the claimant company might result in oppression, in that the claimant company would be forced to abandon a claim which has a reasonable prospect of success, the court is entitled to refuse to make that order, notwithstanding that the claimant company, if unsuccessful, would be unable to pay the Defendant's costs (see *Aquilla Design (GRB) Products Ltd. -v- Cornhill Insurance plc*[1988] BCLC, 134, Court of Appeal); (b) Before the court refuses to order security on the ground that it would unfairly stifle a valid claim, the court must be satisfied that in all the circumstances it is probable that the claim would be stifled (see *Keary Developments Ltd. -v- Tarmac Construction Ltd.*[1995] 2 All E.R., 535, Court of Appeal); (c) In all but the most unusual cases,

2.7 Even if one of the conditions is established by the defendant the court retains a discretion whether or not to order security.[5]

(ii) Claimant with ATE Insurance

3. How is the analysis affected where the claimant has the benefit of ATE insurance? The claimant will often say that it is an answer to any application for security: in the event of the claimant losing the policy will respond and pay the defendant's costs. Therefore there is no reason to believe that it will be unable to pay the defendant's costs if ordered to do so and so the relevant condition in r.25.13 is not met.

4. The defendant will typically respond by pointing to the fact that an ATE policy is an inherently uncertain mechanism for payment and does not allay its concerns. ATE policies typically have various clauses allowing the insurer to cancel or terminate the policy and allowing for avoidance for misrepresentation or non-disclosure.

5. So, a typical policy will have terms such as the following, or variations thereon:

> "If the Insured is bankrupt, insolvent or becomes bankrupt or insolvent during the Period of Insurance the Insurer shall have the right to withdraw its support of the Legal Proceedings…."
>
> "Your policy only covers you during the period of insurance and provided that…We believe that it is more likely than not that your claim will be successful."
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> "Failure to keep to any of these conditions may lead the insurer to cancel your policy, refusal to pay or withdraw from an ongoing claim….
>
> …You must
>
> (a) observe and keep to the terms of this policy.

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the burden lies on the claimant company to show that, apart from the question of whether the company's own means are sufficient to meet an order for the security, there will be no prospect of funds being available and forthcoming from any outside source (see *Kufaan Publishing Ltd. -v- Al-Warrack Bookshop Ltd.*, March 1st, 2000, Court of Appeal (unreported))."".

[5] Relevant considerations include:
(1)Whether the claimant's claim is bona fide and not a sham;
(2) Whether the claimant has a reasonably good prospect of success;
(3) Whether there is an admission by the defendants in their defence or elsewhere that money is due;
(4) Whether there is a substantial payment into court or an "open offer" of a substantial amount.
(5) Whether the application for security was being used oppressively, e.g. so as to stifle a genuine claim.
(6) Whether the claimant's want of means has been brought about by any conduct by the defendant, such as delay in payment or in doing their part of any work;
(7) Whether the application for security is made at a late stage in the proceedings.

(b) not do anything that hinders us or the solicitor.

(c) tell us immediately if anything that may materially alter our assessment of the claim…

(e) provide us with everything we need to help us handle any claim…

(i) minimise anything that the insurer has to pay and try to prevent anything happening that may cause a claim under this policy…"

"Termination

The Policy will terminate if the Insured or Solicitor terminates the Conditional Fee Agreement."

"We may cancel the Policy by giving fourteen days' notice in writing to the Insured and Solicitor if….

a) the Insured fails to comply with the terms of the Conditional Fee Agreement;
b) the Insured does not follow the Solicitor's recommendation with regard to the settlement of the Legal Proceedings.
c) the Insured Litigant does not follow Our recommendations with regard to settlement of the Legal Proceedings…"

"In the event that the Policy is terminated or cancelled, the Insurer shall be under no obligation to make any payment."

"Conduct of Legal Proceedings

a) All information to be given to the Solicitor

The Insured must give all information and assistance required by the Solicitor. This must include a complete and truthful account of the facts of the case and all relevant documentary or other evidence in the Insured Litigant's possession."

"This insurance does not cover… Any payment by the Insurer under the Policy where there has been misrepresentation or material non-disclosure by the Insured or Solicitor or if the policy has been obtained by any fraudulent or dishonest means."

6. This is a question which has arisen over the last few years with increasing frequency.

6.1 In *Nasser v United Bank of Kuwait* [2002] 1 WLR 1868 at para. 60, where Mance LJ said, obiter:

> "I would interpose at this point that, even where a claimant or appellant is resident abroad, there may of course be special factors indicating that any order for costs will be satisfied in some other fashion. The interesting possibility was raised before us that a claimant or appellant who has insured against liability for the defendants' costs in the event of the action or appeal failing might be able to rely on the existence of such insurance as sufficient security in itself. I comment on this possibility only to the extent of saying that I would think that defendants would, at the least, be entitled to some assurance as to the scope of the cover, that it was not liable to be avoided for misrepresentation or non-disclosure (it may be that such policies have anti-avoidance provisions) and that its proceeds could not be diverted elsewhere."

6.2 In *Al-Koronky v Time-Life Entertainment Group Ltd* [2006] EWCA Civ 1123 Sedley LJ said:

> "[35]…A claimant who has satisfactory after-the-event insurance may be able to resist an order to put up security for the defendant's costs on the ground that his insurance cover gives the defendant sufficient protection.
>
> [36] In the present case, however, we are told that the claimants have after-the-event insurance, but that the policy is voidable or the cover ineffective if their eventual liability for costs is consequent upon their not having told the truth. We have not been told what the premium was, but since the outcome of this case will depend entirely upon which side is telling the truth, one wonders what use the insurance cover is. If the claimants win, they will have no call on their insurers. If they lose, it is overwhelmingly likely that it will be on grounds which render their insurance cover ineffective."

6.3 In *Michael Phillips Architects v Riklin* [2010] EWHC 834 (TCC); [2010] BLR 569 Akenhead J, having reviewed the decisions in *Nasser*, *Al-Koronky* and another case *Belco Trading v Kondo* [2008] EWCA Civ 205[6], laid down the following principles:

> "[18] These three cases are not absolutely determinative as to whether ATE insurance can provide adequate or effective security for the defending party's costs. That is not surprising because it will depend upon whether the insurance in question actually does provide some secure and effective means of protecting the Defendant in circumstances where security for costs should be provided by the Claimant. What one can take from these cases, and as a matter of commercial common sense, is as follows:

[6] Where Longmore LJ had said , at [9]: "it is most unlikely that any standard form of ATE insurance could provide a suitable alternative to the standard forms of order the security of the costs."

(a) There is no reason in principle why an ATE insurance policy which covers the Claimant's liability to pay the Defendant's costs, subject to its terms, could not provide some or some element of security for the Defendant's costs. It can provide sufficient protection.

(b) It will be a rare case where the ATE insurance policy can provide as good security as a payment into court or a bank bond or guarantee. That will be, amongst other reasons, because insurance policies are voidable by the insurers and subject to cancellation for many reasons, none of which are within the control or responsibility of the Defendant, and because the promise to pay under the policy will be to the Claimant.

(c) It is necessary where reliance is placed by a Claimant on an ATE insurance policy to resist or limit a security for costs application for it to be demonstrated that it actually does provide some security. Put another way, there must not be terms pursuant to which or circumstances in which the insurers can readily but legitimately and contractually avoid liability to pay out for the Defendant's costs.

(d) There is no reason in principle why the amount fixed by a security for costs order could not be somewhat reduced to take into account any realistic probability that the ATE insurance would cover the costs of the Defendant".

6.4 In *Riklin* the judge held that, even though there was no issue of fraud raised in the pleadings, nonetheless where there was a time-claim for work done by architects “it is at least within the realms of possibility that there could be findings of fact that the time claim has been more than insignificantly exaggerated. In those circumstances it could well be open to the insurer to avoid the policy under Clause 8 [of the policy]” In that case the judge found that the ATE policy provided no real security for the defendants’ costs let alone any real comfort for the defendants.

6.5 In *Natas Group Limited (in Administration)* v *Styles and Wood Limited* [2011] EWHC 3464 (TCC) 142 ConLR 178 Akenhead J returned to this issue. The claimant sought to resist an application for security by reference to the ATE Policy it had the benefit of. The judge held that were he to order security the claim would not be stifled. He then went on to consider the significance of the ATE policy. He said this, at [27]:

“The ATE insurance however does provide a degree of comfort, albeit not nearly as much as the Claimant suggests. The £250,000 cover does cover the Defendant's costs but it also covers the Claimant's disbursements. Those were estimated as at February 2011 to include £289,710 for disbursements albeit £127,000 of this relates to the insurance premium. The disbursements exclusive of that premium are some £162,000. It could be said that this net figure is nominally available to cover the Defendant's costs. However, this cover does not

provide anywhere near as good or as certain cover as a payment into court or a bank guarantee, which are the more usual ways of providing security for costs. Genuine concerns and uncertainties relating to this ATE insurance are:

(a) It cannot and should not be incumbent on the Court on a security for costs application to determine with any precision what the insurance policy, properly construed, actually is. What the Court can do is to identify risks and uncertainties and weigh them in the balance on the exercise of the discretion.

(b) Special Condition 1 could be read, in conjunction with Exclusion 9, as meaning that the insurer might not be liable if the Claimant succeeded on a section of its claim, say for instance, the claim identified in Schedule 1 to the Particulars of Claim, but lost overall because there were over-payments or excessive allowances on the other nine heads of claim. It could be read as meaning that, if the Defendant only succeeded on its Counterclaim to the tune of say 10%, there would be no liability on the insurer. I regard this as a not insignificant risk albeit that one would hope that any decent insurer would not take the point. There is no evidence before the Court about the pedigree of this Lichtenstein insurer. Additionally, if there has been or is to be a Part 36 offer made by the Defendant and if it was effective in that the Claimant "won" but did not "beat" the offer, there is an even greater chance that the insurer could argue that it had no liability at all to pay out anything.

(c) The termination Clause 2 is a worrying clause in the sense that there is no definition of what "material development" could lead the Insurer to withdraw the benefit of the Policy. It is highly arguable that a material development might be the discovery that a key witness cannot support, any more, a significant part of the claim or that such a witness is not prepared to co-operate with the Claimant any more. If that is right, the insurers could pull out and the Defendant would be left with no security.

(d) Clause 8[7] has ramifications in respect of and over which neither the Court nor the Defendant can be aware or have any control. The Administrators will have procured this insurance, I presume, on the presentation of evidence and opinion supporting the Claimant's position. Whilst of course the Court does not expect these privileged documents to be put in front of it, it is at the very least reasonably arguable that any material misrepresentation or non-disclosure can lead to an avoidance of the policy, which would be retrospective in effect. It is of

[7] Which provided as follows: "In the event of misrepresentation, misdescription or nondisclosure of any material particular by the Insured in relation to either the formation of the contract of this insurance or the conduct of the Proceedings, the Insurer shall become entitled to avoid this Schedule forthwith upon giving notice of such avoidance to the Insured and the Premium paid to the Insurer shall be forfeited."

course not necessary that there should have been any fraud on the part of the Administrators.

(e) There is at least some confusion in the drafting of the policy as to how the premium is dealt with in circumstances in which there is an overall order for costs against the Claimant. The premium comes into the "deficiency of damages" calculations."

The judge went on to order that the claimant should make a payment into court albeit one which was discounted by a particular amount to allow for two factors: first being "a real chance that some part of the ATE insurance may be available" and the second being the real possibility that the parties would resolve the case amicably.

6.6 A notable shift in emphasis is discernible in the next case, *Geophysical Service Centre Co v Dowell Schlumberger (ME) Inc*, [2013] EWHC 147 (TCC); 147 Con LR 240. That was a straightforward TCC case where a Jordanian company entered into a contract with the defendant in relation to the provision of seismic services to BP in Jordan. The judge, Stuart-Smith J held as follows:

(1) The ATE market had, by 2013 become considerably more mature than when *Nasser* was decided and that the funding of claims by ATE policies was a central feature of the ability of parties to gain access to justice.

(2) The judge then said this, at [15]: "In the absence of evidence to the contrary, the court's starting position should be that a properly drafted ATE policy provided by a substantial and reputable insurer is a reliable source of litigation funding." This is a radical departure from the tone of all the decisions coming before.

(3) He continued, at [20]: "Ultimately, on an application such as this, the question is not whether the assurance provided by an ATE policy is better security than cash or its equivalent, but whether there is reason to believe that the claimant will be unable to pay the defendant's costs despite the existence of the ATE policy. It must now be recognised, in my judgment, that depending upon the terms of the policy in question, an ATE policy may suffice so that the court is not satisfied that there is reason to believe that the claimant will be unable to pay the defendant's costs." Again, this is a departure from previous approaches which had tended to consider the question of the sufficiency of an ATE policy by way of comparison to cash or a bank guarantee.

(4) In that case the judge took the view that, given the terms of the ATE policy, the defendant had not established that there was "reason to believe" that the claimant would be unable to pay the defendant's costs if ordered to do so. But it is significant that in that policy the insurer's capacity to avoid the policy was limited to non-disclosure or misrepresentation which was fraudulent.

6.7 That shift in emphasis is continued in the most recent cases on the subject.

6.7.1 In *Harlequin Property (SVG) Ltd v Wilkins Kennedy* [2015] EWHC 1122 (TCC); [2015] BLR 469, a professional negligence claim against a firm of accountants, the claimant relied on a policy which exclude the right to avoid for fraud. The only objection which concerned the judge related to the risk of the claimant's insolvency, and the obligation on the insurer to pay out to the liquidators, who might use the sums for distribution *pari passu* to creditors. The claimant was a foreign company and the law governing the place of its incorporation did not have equivalent statutory protection to the UK Third Parties (Rights Against Insurers) Act.[8] The court showed its amenable to entertaining further amendments to the policy to surmount that difficulty.

6.7.2 In *Premier Motorauctions Ltd v Pricewaterhousecooper LLP* [2016] EWHC 2610 (Ch); [2017] Bus LR 490, which was a claim by a company in liquidation, and so brought by its liquidators, the judge applied *Geophyiscal* and declined to order security. It is important to note the judge placed considerable emphasis on the fact that the claimant in that case was effectively the liquidator and therefore it was unlikely that he would have made any misrepresentations or material non-disclosures when seeking to obtain the policy nor was it likely that he would not comply with his ongoing obligations under the policy. I propose to consider some of the judge's reasoning below.

(iii) Overview

7. Where does this leave defendants facing claims by impecunious claimants which have the benefit of ATE insurance? Most significantly it is now clearly established that when considering whether or not to order security the Court should treat the existence of the ATE policy as part of the asset base of the claimant; the question is whether, having regard to the existence of the policy, as part of the totality of the evidence, there is reason to believe that the claimant will be unable to pay the defendant's costs if ordered to do so. That is different to the emphasis in the earlier cases, which was to ask whether the ATE policy was a suitable form of alternative security to cash or a bank guarantee. The modern approach is not to treat the policy as a form of security, but as simply part of the asset picture. As the judge said in *Premier Motorauctions* at [40-41]:

> "I therefore see no reason in principle why the existence of that policy should not be taken into account together with its other assets at the first stage when deciding whether the jurisdiction to make an order for security for costs under

[8] The judge, Coulson J, laid down the following principles, at [22]: "(1) Adequate security for costs can be provided to a defendant by means other than a payment into court or a bank guarantee; (b) Depending on the terms of the insurance and the circumstances of the case, an ATE insurance policy may be capable of providing adequate security; (c) There may be provisions within the ATE insurance policy which a defendant can point to and say that, on the happening of certain events, those provisions may reduce or obliterate the security otherwise provided; (d) In that event, the court should approach such objections with care: in order to amount to a valid objection that an ATE policy does not provide appropriate security, the defendant's concern must be realistic, not theoretical or fanciful.

> CPR 25.13 is engaged. That must be so where the very purpose of such a policy is to provide the means by which the claimant company "is able to pay the defendant's costs if ordered to do so".
>
> Accordingly, I think that in a case in which a claimant has obtained an ATE policy specifically to cover the bringing of a claim, and relies upon it to resist an application for security for costs, the approach taken by Stuart-Smith J in paragraph 20 of *Geophysical* is correct. The question is not whether the ATE policy provides the same security as cash or a bank guarantee, or indeed whether the ATE policy provides the same security as might a deed of indemnity from the same or another insurer. It is whether, having regard to the terms of the ATE policy in question, the nature of the allegations in the case and all the other circumstances, there is reason to believe that the ATE policy will not respond so as to enable the defendant's costs to be paid."

8. Nonetheless the recent cases do not lead to the conclusion that an ATE policy will now always defeat an application for security.

9. *Propensity of insurers to avoid.* Defendants often entertain genuine concerns that in the event of victory the benefit of the ATE policy will prove to be illusory because, rather than have to pay out what may be a very substantial sum of money to indemnify the claimant against its costs liability to the defendant, the insurer will seek to avoid the policy.

10. Stuart-Smith J and Snowden J were sanguine about the propensity, or lack of it, of insurers to avoid policies in the event of the claimant losing the claim: see for instance at [52] of *Premier Motorauctions*. In reality avoidance is a real risk. A good example is *Persimmon Homes Ltd* v *Great Lakes Reinsurance (UK) plc* [2010] EWHC 1705[9] (Comm). This was a case where the claimant (P), had been a defendant to earlier proceedings brought by a claimant (CPH) which was impecunious and whose lawyers were acting on CFAs. CPH also had the benefit of an ATE policy. P defended the claim to trial and was wholly successful. No application for security for costs had been made, even though P's solicitors had written, at an early stage in the proceedings: "We do not regard an After the Event Insurance Policy as being adequate security for costs. One of our fundamental concerns arises out of the fact that such policies normally contain provisions which entitle the insurer to avoid the policy as a result of any material non-disclosure. Our client would have no assurance that grounds do not exist (or will not arise) entitling insurers to avoid the policy."

11. The insurers then declined to make payment under the ATE Policy, citing the findings of dishonesty made by the judge. P wound up CPH and then proceeded against the insurer via the Third Parties (Rights against Insurers) Act 1930 (now replaced by the Third Parties (Rights Against Insurers) Act 2010). The insurers contended that they were entitled to avoid the policy. They were successful. I myself know of other cases where an ATE policy has been avoided after judgment.

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[9] Another, very recent, example is *Denso Manufacturing UK Ltd v Great Lakes Reinsurance (UK) Plc [2017] EWHC 391* (Comm).

12. *Terms of the policy*. It is clear that the detailed terms of the policy will be highly material to the issue. It is likewise clear that those terms will have to be set in the context of the nature of the claim. If the claim is one which involves fiercely contested evidence such that, if the defendant's case prevails, it will mean that the claimant's case is rejected, then the defendant's contention that the policy is liable to avoidance should carry significant force. The postulate of the relevant condition is that the defendant has had an order in its favour for costs; that means it has won; that will in turn mean that, in many cases, the claimant's evidence has been rejected; and that will, finally mean, that the claimant has, at the very least, made a material misrepresentation or non-disclosure to the insurer.[10] Nothing in the recent cases undermines this analysis.

13. A common concern of a defendant is that the policy will be voidable by the insurer for fraud. As to this:
    13.1 Any policy which seeks to exclude the right to avoid for fraud has to do so in the clearest terms: *Candy v Holyoake* [2017] EWCA Civ 92, citing *HIH v Chase Manhattan* [2003] UKHL 6. Therefore a failure to be explicit about this is a ground for arguing the inadequacy of the policy, especially in cases which involve a "swearing match".
    13.2 It is from time to time argued by a defendant that a non-avoidance clause whereby the insurer contracts not to avoid the policy even in the event of fraud on the part of the insured claimant is, even if very clearly drafted, nonetheless void as contrary to public policy. This analysis is now supported by the decision in *Candy* where Gloster LJ said:

> "For present purposes it is sufficient merely to say that there is at least a real prospect that (on the hypothesis that the respondents lose the action and are found to have been dishonest) the insurer could properly argue that there is a rule of public policy which would entitle it to avoid on the grounds of the insured's fraud, regardless of the policy terms. This gives rise to an objectively reasonable appreciation of risk such as to render the policy an unsatisfactory form of fortification….In my judgment it is not appropriate to rule out the possibility of an insurance policy being adequate fortification, even in a case where allegations of fraud were being made against a claimant. For example, it might be thought that a policy which in clear and specific terms waived the duty of disclosure altogether, coupled with an equally clear term and representation by the insurer that it would not avoid for fraud of the insured in presentation of the risk (or any other ground), would be good fortification, notwithstanding any principle of so-called public policy."

14. *Identity of the claimant.* It is clear from the *Premier Motorauctions* claim that the identity of the claimant in that case – an officeholder - was highly relevant to the outcome of the application. Where the claimant is not in liquidation then a defendant

[10] See also the comments of Lord Drummond Young in *Monarch Energy v Powergen Retail* [2006] CSOH 102 at para [28] to the effect that even a conscientious solicitor cannot be certain that he has unearthed all material facts about an action before applying for ATE insurance.

may well be able to argue with greater force that the court cannot disregard the real risk of a later avoidance because it is the claimant, with knowledge of the facts giving rise to the claim, which has made the presentation to the insurer.

15. *The solvency of the insurer*. It is important to consider the identity of the insurer. Is it FSA-regulated; is it well-known in the market; does it have a credit-rating; is it UK-incorporated? In *Premier Motorauctions* the judge was willing accept that there was sufficient doubts about one of the insurers providing cover that a security order would have been justified (no security was in fact ordered at that time for other reasons): see at [72].

16. *Benefit of policy would go to the claimant*. An argument from time to time deployed is to the effect that the proceeds of the policy would pass to the claimant, not directly to the defendant and therefore there is no certainty that it would then be paid over to the defendant in full. Further if the claimant is, or goes into, liquidation, then the proceeds of the policy would fall to be distributed *pari passu* with all the claimant creditors. That argument was rejected in *Premier Motorauctions* on the basis that "where a liquidator has arranged an ATE policy to cover an adverse costs order in a particular case, any payments made by the insurer under the policy would be paid and received by the liquidator upon an implied trust for the sole purpose of paying that costs order and not for the purpose of distribution to other creditors." (see at [66]). On the other hand if the claimant is a foreign company, then this argument may have weight, as we have seen in the *Harlequin* case above

17. *Amount of Cover*. What security is being sought? Is the cover adequate for that?

18. *Offer of Deed of Indemnity*. Sometimes the ATE insurer is willing to issue a Deed of Indemnity, directly addressed to the defendant. That proved acceptable to the Court in *Verslot Dredging v HDI Gerling Industrie Vesicherungag AG* [2013] EWHC 658 (Comm), where the judge said: There is no magic in the provision of security from a first-class London bank. The essential question for the court in deciding on what form of security is acceptable is whether what is proposed does indeed provide real security. This it may do if it amounts to a promise which would in all likelihood be honoured, given by an entity with the wherewithal to pay and against whom enforcement can readily be obtained; in short, if given by a truly creditworthy entity."

19. *Copy of the ATE Policy.* The policy is likely to be of great interest to a defendant. It appears that while there is no general free-standing right to seek disclosure from a claimant who is reluctant to disclose it, nonetheless there are circumstances where it is disclosable under CPR r.3.1(2)(m): see *The RBS Rights Issue Litigation* [2017] EWHC 463 (Ch), at [100]ff, and in particular at [109]:

> "Thus, I accept that generally an ATE policy, which does not impact on the issues in the case now that the premium can no longer be recovered as part of a costs award, will not be relevant. However, there may well be exceptions: for example, where the ATE policy has been deployed in the course of the proceedings whereby to influence or impact on a decision (procedural or otherwise) such as it has been in the present case (see below). That is especially likely, as it seems to me, in the context of group litigation where the

considerable benefit to claimants of several liability has been obtained. More generally, I would add that, to my mind, the court will in such a context tend to be more amenable to such disclosure as the price of the other benefits, and to ensure that claimants themselves have transparency."

The judge also held that privilege did not attach to an ATE policy.

(iv) Security against Litigation Funder

20. There is a little used – until recently - provision in CPR r.25 which allows a defendant to seek security for costs against a litigation funder. R.25.14 provides as follows:

> "(1) The defendant may seek an order against someone other than the claimant, and the court may make an order for security for costs against that person if –
>
> (a) it is satisfied, having regard to all the circumstances of the case, that it is just to make such an order; and
>
> (b) one or more of the conditions in paragraph (2) applies.
>
> (2) The conditions are that the person –
>
> (a) has assigned the right to the claim to the claimant with a view to avoiding the possibility of a costs order being made against him; or
>
> (b) has contributed or agreed to contribute to the claimant's costs in return for a share of any money or property which the claimant may recover in the proceedings; and
>
> is a person against whom a costs order may be made."

21. In the context of this seminar it is sub-para (2)(b) that is relevant and in particular the position of the litigation funder is in focus. The litigation funder will typically agree to fund certain of the costs of the claim (e.g. counsel's fees, expert fees, sometimes solicitor's fees, sometimes adverse costs orders) in return for a share of any damages or other sums awarded. There are no reported decisions of which I am aware where such an order has been made (though it seems that an order was made in the *Sharp v Blank* litigation – see Nugee's judgment at [2017] EWHC 141 (Ch) although the rule has been touched upon in discussion from time to time. A number of questions arise:

    21.1 Where a third party funder is agreeing to fund the claim up to a fixed amount should the security order against the funder be delimited to that amount, in accordance with the principles of *Arkin v Borchard* (discussed below)?

    21.2 If the litigation funder does not comply with the order, what should be the consequence; staying or striking out the claim? (That of course is the usual result where a security order made against the claimant is not complied with.)

22. The fullest and most recent discussions were in *Wall v Royal Bank of Scotland plc* [2016] EWHC 2460 (Comm), and *The RBS Rights Issue Litigation* [2017] EWHC 463 (Ch), decided in the last few months. *Wall* was a claim by an individual to whom causes of action vesting in certain companies had been assigned. The fact of the assignment meant that the claimant was, in essence, immune to an order for security; however the claim was a very substantial one and the claimant, who was on the face of it impecunious relative to the very substantial legal costs which he would have to incur, had the benefit of access to substantial legal resources as well as an ATE policy. The defendant suspected that the claimant had the benefit of litigation funding and wished to make an application under CPR r.25.14. The problem was that it could not mount such an application in the absence of knowing the identity of the funder. The claimant declined to say whether he had the benefit of litigation funding and declined to identify any such funder. The defendant accordingly applied for an order that the claimant identify the funder. The application raised for consideration a number of interesting questions:

23. *Jurisdiction to order claimant to identify any funder in order to allow defendant to make an application*. The judge (Andrew Baker QC, as he then was) had no difficulty in holding that there was implicit in r.25.14 a power to order the claimant to identify a litigation funder, both as to name and address and as to fulfilment of the criteria in r.25.14(2)(b). Without such power the defendant would, in practice, be unable to avail itself of the jurisdiction contained within it: see for instance *Reeves v Sprecher* [2007] EWHC 3226 (Ch)[11]; *Raiffeisen Zentralbank Osterreich Ag v Crossseas Shipping Limited* [2003] EWHC 1381 (Comm); *Abraham v Thompson* [1997] 4 All ER 362.[12] The judge's conclusion was summarised as follows, at [26]:

> "i) Where there is good reason to believe that a claimant has funding falling within CPR 25.14(2)(b), the court thereby has power to grant a remedy by way of security for costs against the funder(s) in question.
>
> ii) For an application to be made for the court to exercise that power, it is necessary to identify the funder(s) in question against whom any application will be made.
>
> iii) Where the defendant does not know that identity, but the claimant does, ordering the claimant to reveal it to the defendant is doing no more than making an order that is necessary to make effective the primary power (to grant a security for costs remedy under CPR 25.14).
>
> iv) The court therefore has power to grant the present application."

[11] At [23], [27]: "In my judgment, it must be right that the Court has, as a power necessarily inherent in CPR 25.14, the power to order disclosure to the defendant in proceedings the identity and address of any third party who has entered into an agreement to fund the prosecution of the action against the defendant within the terms of CPR 25.14….I think that in the absence of any offer of such information from the claimant, the defendants would be entitled to an order from this Court at this stage for disclosure of the identity and address of the third party funder, and the disclosure of the answer to the question whether that third party funder falls within sub paragraph (2) of CPR25.14"

[12] "where the power exists to grant the remedy, there must also be inherent in that power the power to make ancillary orders to make that remedy effective".

24. It should be said that the Court may well, at this preliminary stage, go further and order the claimant to identify whether the funding arrangement which was in place fell within the description at CPR r.25.14(2)(b). But it would be reluctant to order the funding contract itself at this stage, in the absence of the funder before the court.

25. *Art 8 of the ECHR*. The judge was unimpressed by the suggestion that an order requiring identification would infringe the claimant's right to respect for his private life.

26. *Relevance of the ATE policy*. The claimant argued that no order should be made requiring identification of any funder because it was clear that, if a substantive application under CPR r.25.14 were to be made, it would be unlikely to succeed. This was because the claimant had the benefit of an ATE policy which provided adequate protection for the defendant. *Geophysical* was relied upon. The judge was unpersuaded by this, for two reasons:

    26.1 First, he said that different considerations were engaged on an application against a third party litigation funder than against a claimant: "On an application against a claimant, the court must balance the defendant's desire to be paid its costs if it succeeds in the litigation against the fact that an impecunious claimant may be deprived of access to the court if security is required. RBS will submit, says Mr Mitchell, that the position is different in an application against a third party funder buying a stake in the claim or its proceeds: the application is then not against an impecunious claimant seeking to vindicate rights, but against a professional entity seeking to profit from the litigation of others and likely to be well able to secure the defendant's costs. That seems to me a serious and important argument and RBS should have a proper opportunity to pursue it." (at [41]).

    26.2 Secondly, he took the view that, in view of the terms of the policy, it was by no means clear that the ATE policy did in fact provide the protection asserted by the claimant.

27. This approach was endorsed in *RBS*. In *RBS* the grounds of opposition to disclosure of the identity of the funder were that:
    27.1 *RBS had no settled intention to proceed to apply for security for costs against the third party funder*. The judge rejected that ground: a defendant could perfectly sensibly wish to know the identity of the funder and his whereabouts in order to make an informed decision. However the underlying application for security had to be a realistic possibility; i.e. if the appcliation was purely tactical then it would be refused
    27.2 *Any application would be bound to fail.* The judge agreed that that would clearly be a consideration against ordering disclosure. The underlying application had to have at least a realistic prospect of success.

28. The judge in *RBS* made some other helpful comments:

28.1 Any application for costs against funders was **not** a secondary one; their liability under section 51 of the SCA was primary, alongside that of the losing party.

28.2 Security against funders was contemplated as not an out of ordinary order, given that they would be likely to be well able to meet it and their interest in the litigation was purely commercial.

28.3 It was contemplated that any order for security against a funder would provide that the action would be stayed if the security were not put up; i.e. the claimants would be prejudiced by a failure of their funders to comply.

B. Proceedings are Concluded

(i) The Defendant succeeds

29. We now scroll forward to the situation where the defendant has succeeded at trial or otherwise and an order for costs has been made in its favour. The claimant is unable to meet that costs order through his own resources. What avenues for recovery are available to the defendant?

30. Of course the defendant may have obtained security for costs under either or both of the routes discussed above. That security may go some way to discharging the costs incurred by the defendant. But it will rarely go the complete way.

(ii) Pursuing the ATE insurer

31. The reality is that there is a substantial prospect of the insurer seeking to avoid cover. This will often be founded upon the terms of the judgment: the Court may have decided that the claimant's witnesses were not telling the truth; it may find that the claim was wildly exaggerated. This may provide valuable material to the insurer. In such circumstances, if the insurer avoids cover, the defendant will have to pursue a subrogated claim via the Third Parties (Rights Against Insurers) Act 1930/2010. Of course in that case the defendant will be placed in the shoes of the claimant and will be in no better position that that claimant. Such a claim may well be fraught with difficulty: compare the *Persimmon* and *Denso* cases above.

(iii) Costs order against the Litigation Funder

32. **The backdrop.** By section 51 of the Senior Courts Act 1981 and CPR r.46.2 the Court has a jurisdiction to make a costs order against a person who is not a party to the proceedings. This jurisdiction was considered in the leading decision of the Court of Appeal, *Symphony Group Plc v Hodgson* [1994] QB 179 , CA, where it was stated that an order for the payment of costs against a non-party was exceptional (which means simply outside the ordinary run of cases) and should be treated with considerable caution; and that the applicant should warn the non-party at the earliest opportunity of the possibility that such an application might be made. A failure to do so would be relevant to the court's exercise of discretion.

33. In the later decision of the Privy Council in *Dymocks Franchise Systems (NSW) Pty Ltd v Todd* [2004] 1 W.L.R. 2807 it was held that although it will be rare for a "pure

funder" of litigation, with no personal interest in its outcome, to have a non-party costs order made against him, nonetheless where the non-party not merely funds the proceedings but substantially also controls or at any rate is to benefit from them, justice will ordinarily require that, if the proceedings fail, he will pay the successful party's costs. The non-party in these cases is not so much facilitating access to justice by the party funded as himself gaining access to justice for his own purposes.

34. ***Arkin v Borchard***. Then, in the landmark decision of *Arkin v Borchard Lines Ltd* [2005] 1 WLR 3055 the Court of Appeal decided that a third party litigation funder could be liable under section 51(3) of the Senior Courts Act 1981 to pay costs to the successful defendant even where it had been guilty of no impropriety or active involvement in the proceedings. The key statement of the law was as follows:

> "[38] While we do not dispute the importance of helping to ensure access to justice, we considered that the judge was wrong not to give appropriate weight to the rule that costs should normally follow the event In our judgment the existence of this rule, and the reasons given to justify its existence, render it unjust that a funder who purchases a stake in an action for a commercial motive should be protected from all liability for the costs of the opposing party if the funded party fails in the action. Somehow or other a just solution must be devised whereby on the one hand a successful opponent is not denied all his costs, while on the other hand commercial funders who provide help to those seeking access to justice which they could not otherwise afford are not deterred by fear of disproportionate costs consequences if the litigation they are supporting does not succeed.
>
> ….
>
> [40] The approach that we are about to commend will not be appropriate in the case of a funding agreement that falls foul of the policy considerations that render an agreement champertous[13]. A funder who enters into such an agreement will be likely to render himself liable for the opposing party's costs without limit should the claim fail. *Our approach is designed to cater for the commercial funder who is financing part of the costs of litigation in a manner which facilitates access to justice and which is not otherwise objectionable*. Such funding will 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.
>
> [41] We consider that *a professional funder who finances part of a claimant's costs of litigation, should be potentially liable for the costs of the opposing party to the extent of the funding provided*. The effect of this will of course be that if the funding is provided on a contingency basis of recovery, the funder will require, as the price of the funding, a greater share of the recovery should the claim succeed. In the individual case, the net recovery of the successful claimant will be diminished. While this is unfortunate, it seems to us that it is a cost that the impecunious claimant can reasonably be expected to bear. Overall justice will be better served than leaving defendants in a position where they have no right to recover any costs from a professional funder

[13] Champerty involves wanton intermeddling in litigation for profit.

whose intervention has permitted the continuation of a claim which has ultimately proved to be without merit.

[42] If the course which we have proposed becomes generally accepted it is likely to have the following consequences. Professional funders are likely to cap the funds that they provide in order to limit their exposure to a reasonable amount. This should have a salutary effect in keeping costs proportionate Professional funders will also have to consider with even greater care whether the prospects of the litigation are sufficiently good to justify the support that they are asked to give. This will also be in the public interest.

[43] In the present appeal we are concerned only with *the professional funder who has contributed a part of a litigant's expenses through a non champertous agreement in the expectation of reward if the litigant succeeds*. We can see no reason in principle, however, why the solution we suggest should not be applicable where the funder has similarly contributed the greater part, or all, of the expenses with the action." (emphasis added)

35. Those paragraphs set out a relatively clear and simple principle which should usually be capable of being applied without significant difficulty. It should however be noted that there have been extra-judicially made suggestions by Jackson LJ that the *Arkin* cap should be abolished and that funders should be potentially liable for the totality of the defendant's legal costs. As yet no court has said that; and of course there is binding Court of Appeal authority which asserts the reverse; so the change would have to be legislative or made by the Supreme Court. In *Tinseltime Ltd v Roberts & Ors* [2012] EWHC 2628 (TCC) the judge followed *Arkin* notwithstanding a submission founded upon Jackson LJ's extra-judicial statements.

36. The Court in *Arkin* was at pains to distinguish the case where a funder had gone beyond the bounds identified in that judgment; e.g. had started participating in the running of the case. In such a case its costs liability is at large, even where no impropriety is shown: for an example see *Merchantbridge & Co v Safron General Partner 1 Ltd* [2011] EWHC 1524. A case on the other side of the line was *Gulf Azov Shipping Co v Idisi* [2004] EWCA Civ 292.

37. ***Excalibur Ventures.*** *Arkin* was most recently considered in the extraordinary case of *Excalibur Ventures LLC* v *Texas Keystone Inc* [2014] EWHC 3436 (Comm). The claimants had brought extravagant claims alleged to be valued at well over $1.6billion. There was no ATE insurance in place but the claimants had the benefit of very complex arrangements with a number of litigation funders who had paid out £millions (both towards the claimant's legal fees and to meet orders for security for costs made against the claimant) to take the claim to a very lengthy trial in return for a share in any proceeds of the claim. The claims failed catastrophically. The defendants were award costs on the indemnity basis. Although substantial security had been paid into court by the claimant (which was itself funded by the funders), which the defendants of course took the benefit of, the defendants nonetheless applied against the funders in respect of the shortfall, which was estimated to be about £4.8m, and which in the main represented the difference between a costs order in favour of the defendants on the standard and on the indemnity basis.

38. In Christopher Clarke LJ's judgment he decided a number of points which had remained outstanding post-*Arkin*:

38.1 The fact that the security for costs turned out to be inadequate was not a ground for declining to make a non-party costs order: in the fact the reverse was the case (see at [57]). (*Petromec v Petroleo Braisleiro Petrobas* [2006] EWCA Civ 1038 at [14] per Longmore LJ; and *Dolphin Quays Developments v Mills* [2008] 1 WLR 1829 at [62] per Lawrence Collins LJ)

38.2 The *Arkin "*cap" was applicable. It might have been different had the funders behaved dishonestly or improperly (e.g. by seeking to influence or take control of the litigation): but that was not this case.

38.3 However here the *Arkin* cap should be calculated not simply by reference to the payments made by the funders towards the claimant's own costs but also by reference to the amount paid in by way of security. So if a funder had paid £3million towards claimant costs and £3million to meet a security for costs order made against the claimant then its potential liability to the defendant was £6million. See at [134]:

> "The function of the cap is to limit the costs which the funder has to pay by reference to the money that he has put up to finance the action. He should be required to pay the successful defendant no more than he was prepared to put up in relation to the action himself. The cap bears no necessary relationship to the costs which the Defendants have incurred so as to fall to be reduced to the extent that they are covered. The fact that there is security for those costs will, of course, reduce the amount that falls to be paid subject to the cap."

(By contrast the submission of one of the funders was its liability to the defendant should be pro tanto reduced by the amount it put up as security: so that, on the example given above, its liability would be zero).

38.4 Where costs had been awarded against the claimant on the indemnity basis the funders should be liable on the same basis (subject to the *Arkin* cap). Although the funders were not guilty of impropriety they should be at risk given that they entrusted the action which they funded to the solicitors and claimant whose conduct was itself criticized (at [110]).

38.5 The timing of the payment made by the funder in the course of the litigation was a relevant consideration. A funder could not be liable under section 51 for costs incurred by the defendant prior to his funding being provided.

38.6 The court could make an order under section 51 against the parent of the funder where the parent was the true origin of the funds (albeit channelled through the subsidiary) and was the ultimate beneficiary thereof.

39. Christopher Clarke LJ's judgment was endorsed on appeal: see at [2016] EWCA Civ 1144.

(iv) Current practice and issues

40. The following practical points should be noted:

    40.1 It is always advisable to put a funder on notice of a potential claim as soon as possible.[14] Failure to do so could undermine a subsequent application.

    40.2 The application will necessarily be made after a costs order has been made between the parties and usually after the claimant has not complied with it. The procedure is by way of application notice back to the trial judge and will be a summary one, without pleadings.

    40.3 The Court will be prepared in an appropriate case, after a costs order has been made in favour of the defendant, to make a disclosure order to ascertain the existence of a funder or for provision of the funding arrangements: *Flatman v Germany* [2013] 1 WLR 2676, following *Thomson v Berkhamstead Collegiate School* [2009] Costs LR 859.

41. In a recent application in which I was involved, which settled on the door of the court, the litigation funder raised a whole host of arguments with a view to resisting a third party costs order under the *Arkin* principle. This gives one an indication of the type of points the funder might take:

    41.1 *Failure to obtain security for costs.* That was a case where the claimant was a company without assets which had the ostensible benefit of an ATE policy. The defendant had not sought security (I was not instructed until after the trial) and had gone on to win decisively at trial.

    41.2 *Causation*. If the funder in question had not funded the case another one would. Therefore the hurdle of causation had not been surpassed.

    41.3 *Public benefit.* Litigation funding is a positive feature of the procedural landscape, providing access to justice, and nothing should be done which undermines the willingness of funders to assist claimants.

    41.4 *ATE Policy*. The existence of an ATE policy should relieve the funder of its potential liability under *Arkin*, regardless of whether that policy has responded.

C. Potential Professional Liabilities

[14] See *Myatt v National Coal Board* [2007] 1 WLR 1559.

42. Many professional negligence claims have the benefit of ATE insurance and/or litigation funding. It is also worth briefly noting the potential for professional liabilities to arise in relation to funded situations. The most obvious scenarios are:

42.1 A defendant is faced with a claim by an impecunious corporate claimant supported by an ATE policy. No security for costs application is made. The case goes to trial and the defendant is successful. The ATE insurer avoids cover and the defendant's victory is soured by the fact that it has incurred a substantial costs bill which is not going to be met by the claimant or its insurer. In such a situation there may well be a claim against the defendant's solicitor/counsel for failing to make a security for costs application at an early stage of the litigation.

42.2 An impecunious claimant brings proceedings. Its solicitor is tasked with locating litigation funders. The solicitor "pitches" the claims to potential funders and gives advice concerning the underlying merits. In reliance thereon a funder agrees to participate in return for a share in the winnings. The claim fails. The solicitor may be liable to the funder for giving negligently optimistic advice as to the merits of the claim and for failing to advise the funder as to its potential liability in costs under the *Arkin v Borchard* principle. It was reported that a substantial professional negligence claim was intimated (and subsequently settled) by one of the funders in the *Excalibur* case.

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