

Third Party Funding in India

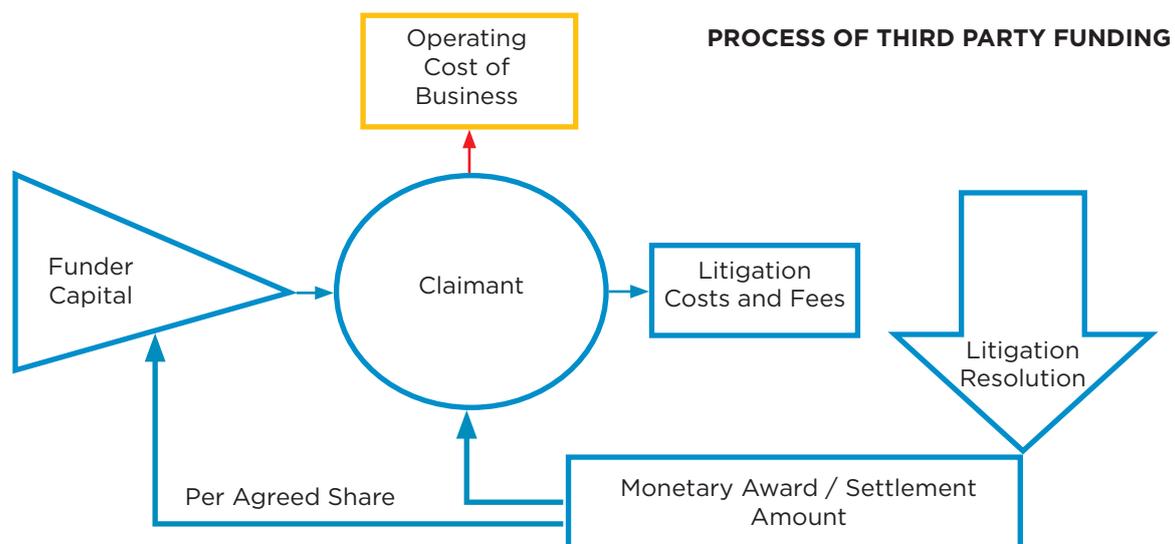


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What is Third Party Funding?

Third Party Funding (“TPF”) also known as Litigation financing, is the non-recourse funding of litigation costs of a party by a funder in exchange for a share in the monetary award of the litigation, if successful. TPF may cover the costs of any kind of dispute resolution mechanism, be it traditional litigation in courts, arbitration and/or mediation. Litigation financing is a manner of leveraging capital while the dispute is ongoing and is often considered to level the playing field between the parties in a dispute.



Who can be funded?

Generally, claimants (which could include counter claimants) are the recipients of TPF as they may receive a monetary award in the case of a successful outcome, since third party funding is premised on a contingent share in such monetary award. There is however an upcoming trend for insurance and other risk transfer arrangements for both claimants and defendants.

Who are the funders?

In addition to specialized third party funders, investment banks, hedge funds, insurance companies and pension funds also invest in legal claims as an asset class. Funders may have ready investible capital or may raise funds for specific claims in an ad hoc manner. Increasingly, litigation financiers are leveraging technology to provide for crowdfunding platforms for TPF. The largest TPF funder in the world has an investment portfolio of approximately USD 2.4 Billion with a market capitalisation of

approximately USD 3.2 Billion. In India, while the large global funders are yet to establish a local presence, today there is at least one crowdfunding platform for litigation financing.

What costs would TPF typically cover?

TPF can cover legal counsel’s fee, court/ tribunal’s fee, cost of expert witnesses, pre-deposit, adverse costs order, and other dispute-related expenses. A 2015-16 survey found that litigants spend up to INR 30,000 crores on legal costs in lower courts alone.

What kind of disputes are funded?

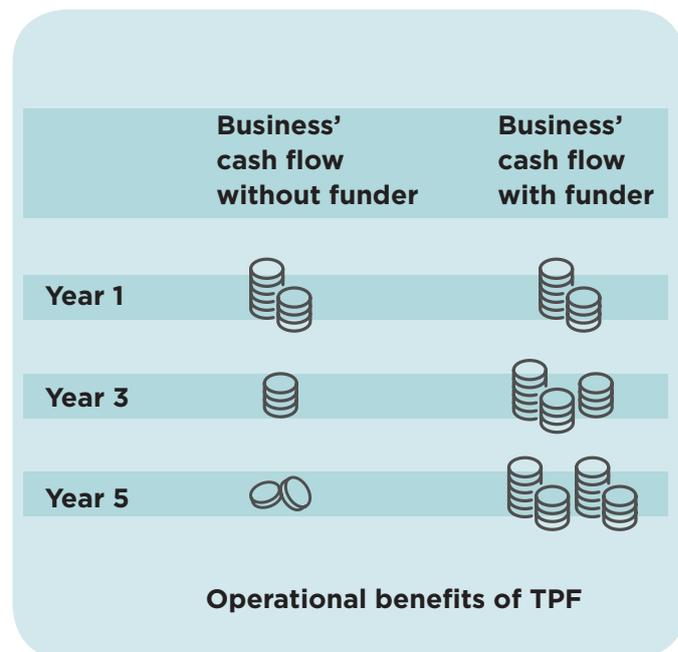
Disputes that attract TPF generally include commercial contracts, international commercial arbitration, class action suits, tortious claims like medical malpractice and personal injury claims, anti-trust proceedings, insolvency proceedings, and other like claims that have a calculated chance of resulting in a substantial monetary award.



The business case for Third Party Funding

Party's Perspective

- Leverage capital to enforce rights
- Allows the funds released to be used for core business (rather than expenditure on legal costs)
- Enables pursuing claims that otherwise would not be brought
- Non-recourse finance with zero cost of capital results in increased operating profit and market value without any impact on EBITDA
- Objective analysis of the dispute from the funder can bolster assessment of “winnable” claims
- Balances bargaining power between parties and encourages settlement driven by merits of the case and not by imbalance in risk tolerance
- Discourages deep-pocketed parties from “gaming” the system by burying the counterparty in paper
- Benefits from the experience and expertise of a repeat-player in the litigation market, including the funder’s ability to ensure greater discipline from lawyers and other intermediaries
- Assists in managing risks of litigation



Stellar Returns

Litigation finance has outperformed on a multiple of invested capital basis



Note: Average of last reported data, Goldman forward multiple of invested capital estimates for leading listed sector players.

Source: Goldman Sachs, Bloomberg

Bloomberg

Funder's perspective

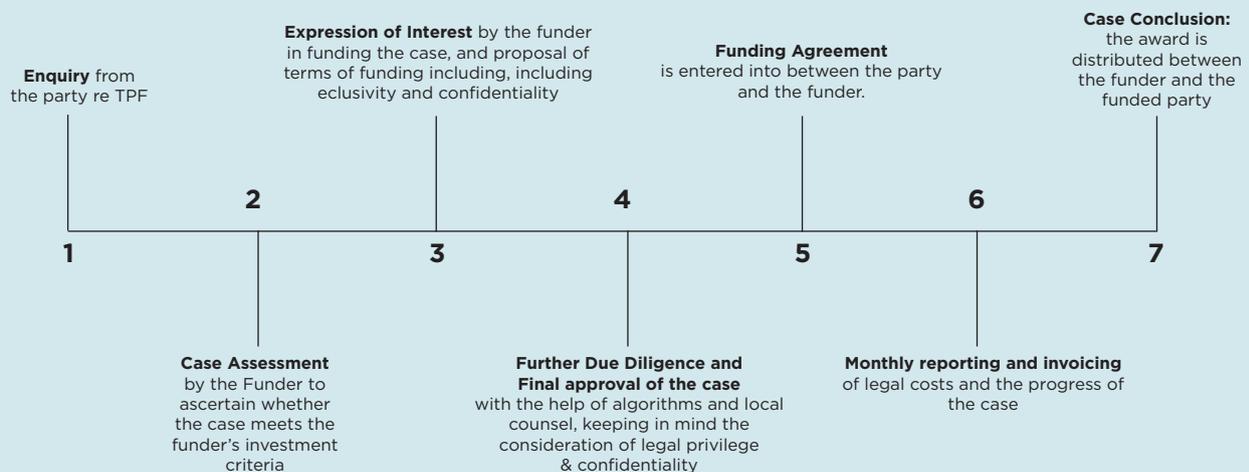
- Bloomberg reports high comparative return on investment
- Distinct asset class allows for diversification as investment returns are not subject to the vagaries of the financial market
- Support cause based funding
- Underexplored market that can effectively deploy capital

Third Party Funding

System's perspective

- Enhances access to justice
- Allows better enforcement of rights, holding accountable those responsible for wrongful acts
- Parties settle based on the merits of the claim and not based on cost or risk-tolerance factors
- Litigation is a chessboard to infinity that results in an unfair advantage to the financially stronger party. TPF enables creation of a financial level playing field between parties, alleviating this structural concern

Raising Third Party Funding - a brief overview of the process





Standard terms of the funding agreement

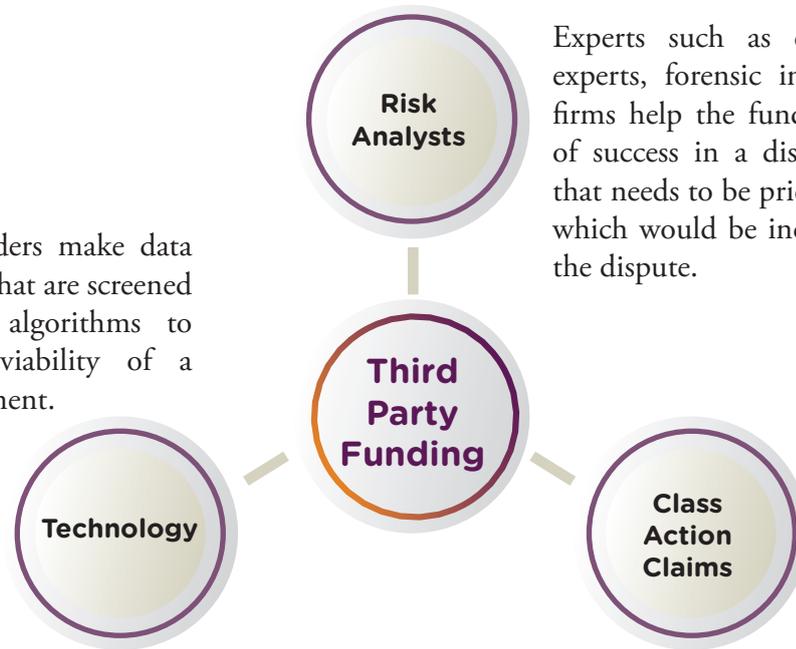
1. **Duties of the Party:** To carry out all necessary acts with reasonable care and skill; to continue diligently with the advice of the lawyers; to cooperate with the funder; to request consent of the funder where its required to incur costs, dispose of claims, discontinue the proceedings, enforce the judgment; to report all material events to the funder, etc
2. **Duties of the Funder:** To review the case; to cover the agreed costs; etc. In some jurisdictions, funders may also have the duty to liaise with the lawyers
3. **Distribution of proceeds following successful claim:** Includes the waterfall of distribution of a successful claim, the definition of proceeds, set-off rights etc. While the stake of the funder is a matter of commercial negotiation, several funds indicate the range of their stake upfront, subject to the risk assessed for each case
4. **Representations by the Party:** Fundamental conditions including the rights of assignment, presence of counterclaims, validity of documents provided, etc
5. **Representations by the Funder:** Funder's capital adequacy, lack of any relationship with the counter-party, independence regarding the merits, no interest in the merits of the dispute, etc
6. **Assignment of Claims to Funder as security:** The details of assignment of rights to claim costs and all subsidiary rights to the funder. In some agreements, funders may seek the right to on-sell
7. **Termination:** The events and circumstances upon which the Agreement can be terminated and its consequences
8. **Settlement proposals by court or opponent:** Stipulations as to the plan of action in the case of a settlement proposal, its acceptance, termination, continuance of proceedings etc
9. **Confidentiality and Disclosure:** Explains the confidential nature of the agreement, for example: the existence of the funding and the identity of the funder, the background of the claim; the procedural status of the claim; the planned strategies and the tactics, the expected recovery, billing arrangements, litigation risk, etc. Agreed process for disclosures where required under law or by regulator
10. **Data transfer by Funder to third parties:** The circumstances when transfer of data by the funder to any other third party (example, witness, expert, insurance companies, etc.) would be permissible



Third Party Funding

Ecosystem supporting TPF

Increasingly, funders make data driven decisions that are screened by confidential algorithms to determine the viability of a dispute as investment.



Experts such as claim assessors, technical experts, forensic investigators and local law firms help the funder determine the chances of success in a dispute, understand the risk that needs to be priced, and ascertain the costs which would be incurred in the resolution of the dispute.

Class action suits and similar disputes that result in blockbuster payouts (by volume of claims), make for attractive investments. Funders often add value as a coordinating platform for such cases.

Factors underlying a TPF investment decision





Third Party Funding: a global snapshot of marquee investments

VANNINCAPITAL

2017: Australia - Vannin funded an AUD 100 million class action against online retailer Surfstitch for being in breach of its continuous disclosure obligations and engaging in misleading conduct. The case is ongoing.

2018: USA - IMF Bentham, Johnson Winter and Slattery Lawyers have collectively funded a class action arising from the Facebook privacy breach where data of about 50 million users was harvested by 'This is My Digital Life' and made available to Cambridge Analytica without users' consent. IMF Bentham allows users to understand whether they have been affected and should join as plaintiffs in the class action suit through a savvy online tool. The case is ongoing.



Burford

2018: USA - Burford Capital has earmarked a USD 50 million pool of capital for financing commercial litigation matters led by women under its Equity Project. In its words "We want to use our assets—our decade of experience, sizable capital and skilled team—to help balance the scale and promote women in law."

2016: Australia - Harbour Litigation Funding funded an AUD 200 million class action against PTTEP Australasia (Ashmore Cartier) Pty Ltd, on behalf of Indonesian seaweed farmers to hold PTTEP responsible for uncontrollably spewing oil and gas into the Timor Sea for more than 70 days in 2009. The case is ongoing.



citigroup

2010: USA - Citigroup backed finance company made USD 11 million profit on a USD 35 million investment in class action lawsuit brought by workers who developed illnesses working at Ground Zero, following the September 11, 2001 terrorist attacks.

2016: Legalist uses algorithms to identify cases suitable for funding, and focuses on smaller-sized cases ranging "from local ice cream manufacturers, bakeries, family-owned vineyards, small toymakers who simply don't have the resources to see cases through. The cases are often against deep-pocketed clients and vendors who have damaged their business and believe they'll get away with it."

Legalist



2018: Canada - Augusta funded class actions against mining company BHP and the labour contractors it used to employ workers. The claims demand compensation and penalties on behalf of workers, alleging that the workers were deliberately hired as 'casuals' when they were regular workers.

2016: India - Advok8, a start-up in India aims to create a market for third party funding by assisting litigants in raising funds for their lawsuits through technology-enabled crowdfunding. From publicly available information, funding has been completed for eight cases.



Third Party Funding

Legal Landscape In India

TPF is not alien to the Indian legal market. Many a *mukadma* (case) have been bought and sold in the unorganised market by opportunistic investors and desperate litigants, often resulting in the transfer of the very asset that is the subject matter of the litigation. Formal arrangements built on risk-reward share on an arms-length basis, as discussed in this paper, are however yet to come of age in India.

Legislative and Judicial Recognition of TPF

In 2015, the Supreme Court in *Bar Council of India v. AK Balaji*, clarified the legal permissibility of TPF in litigation and observed that “There appears to be no restriction on third parties (non-lawyers) funding the litigation and getting repaid after the outcome of the litigation.”.

As on date, there is no legislative instrument that regulates such funding. However, the (Indian) Code of Civil Procedure, 1908 as amended by a few Indian states including Maharashtra, Karnataka, Gujarat and MP, expressly acknowledges the role of the financier of litigation costs of a plaintiff and sets out the

situations when such financier may be made a party to the proceedings. TPF has also received favourable reference in the report of the High Level Committee to review the Institutionalisation of Arbitration Mechanism in India (2017).

Limitations under existing legislative framework

It is well established that lawyers in India are expressly barred from funding litigation when representing the disputing party or accepting a success based fee. This could bear an inherent structural limitation for funders that typically seek contingency fees of legal counsel as a core factor to an investment decision to ensure alignment of interests.

Additionally, whether a TPF arrangement falls foul of public policy would depend on the terms of the arrangement including the funder’s stake in the award, if determined to be extortionate.

Another limitation that is yet to evolve is the permissibility of foreign investment in third party funding of disputes in India.

Notable gaps in the Indian market

Indian litigation is an ever expanding market with increased commercial activity. While there is a demonstrable demand for structured and professional TPF to facilitate the pursuit of viable claims, a few sticky areas of concern are:

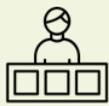
- › Class actions suits or representative claims which provide high likelihood of exemplary damages that attract funders have not gained traction in India. Further, there is hardly any precedent in India for grant of exemplary or ‘blockbuster’ damages for commercial disputes.
- › Funders often use historical data to carry out a risk-assessment analysis before taking up

a case. Such relevant data is a work in progress in India and will take a few years to consolidate.

- › Factors like roster changes during the progress of the case lead to an inherent unpredictability in the system that is not conducive to risk assessment.
- › Funders often prefer sharing the risk of their investment with lawyers appearing for the funded party, by requiring the lawyers to work on a contingency fee basis. This aligns the incentives of the lawyers and funders. This practice is impermissible in India.



Upcoming global trends in Third Party Funding

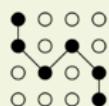


Innovative Risk Transfer Arrangements

Funding arrangements for defendants involve cases where the defendant does not want to bear the upfront costs of litigation, but will pay out-of-pocket, a share of the perceived value of a successful defence, upon dismissal of the claim. Increasingly, defendants not only want the litigation-related expenses funded, but also the risk of an adverse decision transferred. For this, the market is evolving instruments that provide insurance and other arrangements (like “After the Event (ATE) Insurance”) that transfer the risk of a dispute for an upfront price paid by the party.

Increasing legislative sanction for Third Party Funding

Beginning with Australia, many countries are moving away from the outdated common law concepts of champerty, barratry and maintenance, and have legalized third party funding. Most recently, Singapore introduced the amended Civil Law Act and the Civil Law (Third-Party Funding) Regulations, 2017 making third party funding in international arbitration and related proceedings legal. On the same lines, Hong Kong enacted and amended its legislative framework to enable third party funding in arbitration and mediation.



Artificial Intelligence Driving Investment Decisions

Artificial Intelligence enabled algorithms are increasingly being used to determine the outcome of disputes, and to analyse and price the risk in funding a case. For instance, Legalist, a tech third party funding company, uses an Algorithm that determines the chances of winning the case using its database of 10 million court cases before investing.



Portfolio Funding and other evolving structures

In Portfolio Funding, a number of claims brought by a single claimant against the same or different defendants are funded. This helps the claimant get more favorable terms since the funder’s investment and return is spread across the claims, minimizing exposure to a single claim.

Funders are also being approached for transactions like early payment to creditors of an insolvent company who would otherwise have to wait for the conclusion of a claim before being paid, accelerating the proceeds of a settlement, and even funding the costs of business, which might be dependent on a successful claim.

INDIA 2025: CRYSTAL BALL GAZING

1. Legislative acknowledgement of TPF
2. Increased reliance on TPF in commercial disputes including on account of shareholders urging a risk transfer model for litigation.
3. Adoption of a self-regulation model like the United Kingdom. Factors for consideration are:
 - a. Regulation of interference of a funder in the litigation strategy
 - b. Provision for disclosure of funding for all kinds of dispute resolution mechanisms
 - c. Framing of rules concerning confidentiality of the communication between the funder and the litigating party
 - d. Specific disclosure requirements and protection of disclosed documents by litigation privilege
 - e. Validity and legal recognition of contingency fee as a valid legal fee model
4. Foreign capital permitted for domestic TPF by regulatory amendment.

Managing Partner's note on ethical considerations in Third Party Funding

Given the increasing global presence of TPF, we can reasonably expect the Indian landscape to evolve quickly and favourably to support this innovation in dispute resolution. While it espouses several benefits that have been discussed in this paper including levelling the field and increasing access to justice, I do want to take a moment to consider, and give primacy to, the ethical considerations that should underlie the Indian regime for Third Party Funding.

A 1876 Privy Council decision in *Ram Coomar Coondoo v. Chunder Canto Mookerjee*, provides guidance in this regard, where the Court permitted TPF on the grounds of promoting access to justice, but held that *“agreements of this kind ought to be carefully watched, and when found to be extortionate and unconscionable, so as to be inequitable against the party; or to be made, not with the bona fide object of assisting a claim believed to be just, and of obtaining a reasonable recompense therefore, but for improper objects, as for the purpose of gambling in litigation, or of injuring or oppressing others by abetting and encouraging unrighteous suits, so as to be contrary to public policy, effect ought not to be given to them.”*

Delineating clear objects of the participants in the financing arrangements, adopting transparency of funding process and avoiding conflict of interest is essential to the ethical discussions. I emphasise this because, first, the interests of the litigating party, its lawyer and the funder may diverge from one another. The balance further wavers when the funder seeks to put itself in the driver's seat, controlling the litigation strategy and funding the lawyer's fee. While the

lawyers are bound by rules of professional conduct that seek to align their interests with the client, funders are not so obligated. Second, a funder's fiduciary and contractual relationship with its investors deepens this conflict. Third, funders are repeat players, funding a portfolio of cases, whereas the litigating parties are usually one-time players interested in the outcome of only their case.

These conflicts become particularly acute at the time of the negotiation of the funding agreement, and the timing and value of a settlement. For instance, when the settlement amount is lower than the return upon the continuation of the case in courts, the funder might not want to settle the case, even though a party might want otherwise.

In addition to the above, TPF might potentially lead to issues concerning confidentiality and litigation privilege. The litigating party might risk waiving the attorney-client privilege by sharing confidential case-related information with a third party funder. That said, these concerns similarly resonate in arbitration. The contract terms will have to be drafted keeping in mind protection of such privilege.

While these concerns have for long restricted the development of litigation financing, it is heartening to note that the focus has now shifted to regulating TPF, such that the drawbacks arising out of these ethical considerations are balanced against the benefits of TPF. I am confident that India will also embrace an appropriately balanced version of this tool soon.

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This article is not intended to serve as legal advice and the position of law expressed in the article is only valid as on 20th February 2019.



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