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A Measure of the Viability of Third-party Litigation Funding in India

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ABSTRACT

The emergence of Third-Party Litigation funding in India could turn out to be the cardinal tool for shepherding justice that has yet to have taken hold in the sub-continent. Third-Party Litigation funding (TPLF) is a form of non-recourse financial support for funding the litigation, mediation, or arbitration costs of a litigating party, in exchange for a part of the damages awarded from the completion of the litigation if the case is won. TPLF has undergone constant change over the years of its practise and has seen gradual acceptance world-wide even though it was met with disdain and restrictions initially.

TPLF has been sought after by cash-strapped companies who were struggling to continue operations as well as fighting multiple legal battles. TPLF allows companies to essentially create a win-win situation for themselves. If the funded litigation is successful, the company receives a sizeable percentage of the awards and if the litigation is unsuccessful, the company will have not incurred any expenses either way, as the duty to pay for legal representation and other costs was on the funder and not the litigant. The Opponents for TPLF have called out for the banning of this practise as it can give rise to the abuse of the legal process and a possible increase in frivolous lawsuits. Although there has been negligible growth in India in regards to the TPLF market, it is well-established in other common-law countries across the world such as the U.K., Australia, U.S., Canada, etc.. The industry has seen year-on-year growth from its genesis during the 1990's to be currently evaluated at over USD 50 billion- USD 100 billion worldwide. With a plethora of hedge funds and private equity firms exploring new investment classes that does not revolve around the global equity markets, it seems India is poised for an explosion of TPLF in the ensuing decade. This paper seeks to act as a comprehensive guide on TPLF, as well as providing a brief outlook on the status of third-party funding in other countries, Further, it discusses the challenges and legal barriers TPLF will face in the Indian subcontinent. Finally, it seeks to answer the question of how truly viable is TPLF in the Indian realm.

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I. Introduction

A TPLF agreement is usually drawn up between a litigant or class of litigants (class action) and an unrelated party to the litigation, who acts as the funder or it can also be a group of funders. The funder offers to pay for the litigation expenses, court costs, expenses for procuring necessary witnesses and any other dispute related expenses in exchange for a percentage of the damages awarded if the litigation is successful. Non-recourse implies that unlike a loan, the litigating party does not have to pay the funder anything if the claim is not successful.[2]

The non-recourse nature of the agreement makes it undoubtedly more enticing for financially ailing companies rather than accruing more traditional debt or financing legal claims through the sale of shares or debentures of the company.[3]

TPLF as a practise helps alleviate the risk associated with the unpredictable nature of litigation. Even though, TPLF first came into practise in the specific domain of insolvency in the 1990's in Australia, currently it has expanded to the rest of the common law countries as well as gaining a foothold in European civil law countries like Germany, Switzerland, Netherlands, etc. It has also grown to other fields of law in commercial litigation.[4] There are overbearing costs associated with litigation, which acts as a barrier for claim-holders who wish to enforce their rights through the justice system. In the commercial realm, a legal battle against a MNC (Multi-National Corporation), who will have surplus cash reserves and a team of dedicated legal counsels, has to be deliberated thoroughly as the litigation would be long and arduous which would be much more burdensome on a smaller entity if it chooses to pursue justice.[5] In essence, the costs connected to litigation is no different than the costs needed for any other business activity and while there are entities that invest or provide loans for any other activity, there has been a lack of funding available for the costs and risks of litigation. Before the advent of TPLF, risk sharing in lawsuits can only be done either through contingency fees (contingency fee is a payment model wherein the services of a lawyer is procured under the agreement that the lawyer would only be paid from a percentage of the award if the claim is won, if the claim is lost the lawyer does not receive any compensation

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2 Stuart L. Pardau, *"Alternative Litigation Financing: Perils and Opportunities."* UC Davis Bus. LJ 12: 65 (2011).
3 Bedi, Suneal, and William Marra. *"The Shadows of Litigation Finance."* Vanderbilt Law Review, Forthcoming (2020).
4 De Morpurgo, Marco. *"A Comparative Legal and Economic Approach to Third-Party Litigation Funding."* Cardozo J. Int'l & Comp. L. 19: 343(2011).
5 *Ibid.*

for his work) as available in the U.S. and Canada,[6] or sale of a legal claim through securitization, either privately or via the publicly traded stock market, which famously occurred in the Netherlands.[7]

An issue that funders face is how to ensure that the original claim-holder remains cooperative and interested in the suit after the commencement of the funding agreement. It can be solved by leaving a substantial portion of the claim with the original litigant. In practise, TPLF firms usually only hold between 20-60% of the claim. Furthermore, funding firms also prefer to invest in claims that rely on documentary evidence rather than witness testimony and for the most part do not invest in claims below the value of $750,000. Funders also retain the right to terminate the financing agreement at any time although by doing so they would be forfeiting the money already funded.[8]

Historically, the action of TPLF would have been deemed illegal and against public policy when the doctrines of maintenance and champerty were introduced in common law as a tort but from the 19th century onwards, the stance on the subject began to change. Maintenance simply means the unnecessary inter-meddling of third parties to a dispute in which they have no interest. While Champerty is considered as an aggravated form of maintenance and refers to an agreement to share the proceeds of litigation between the original litigant and the inter-meddler.[9] These doctrines have eventually been abolished in some provinces in Australia[10], Canada[11] and England[12].

Another rule that has survived the colonial era in India is the loser-pays rule or more commonly known as the 'English rule' or 'cost-shifting'. The loser-pays rule is a principle that mandates that the losing party in a suit reimburses the winner for their attorney fees' and other general costs incurred in the due course of litigation (court costs, printing costs, accommodation costs for witnesses during the evidence stage).[13] This principle is embodied in section 35 of the Civil Procedural Code of India and is aimed at compensating reasonable

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6 *Ibid.*

7 Hodges, Christopher, Stefan Vogenauer *et.al., "The costs and funding of civil litigation: a comparative perspective"*, Bloomsbury Publishing, (2010).

8 Chen, Daniel L., *et.al., "A Market for Justice: A First Empirical Look at Third Party Litigation Funding"* 1077-1078(2012).

9 Meenal Garg *"Introducing Third-Party Funding in Indian Arbitration: A Tussle Between Conflicting Public Policies."*, NLUJ Law Review 6(2) 71 (2020).

10 Maintenance, Champerty and Barratry Abolition Act 1993.

11 Champerty Act, RSO 1897, cl. 327

12 Criminal Law Act 1967, ss.13-14

13 Available at: *https://lawcommissionofindia.nic.in/reports/report240.pdf* (Last visited on March 25, 2021)

litigation expenses incurred by the successful party and not the actual expenses incurred.[14]

However, in practice, the courts in India regularly dispose of disputes with no order as to costs or for the parties to bear their own costs of litigation when the norm in principle ought to be that the loser pays a reasonable amount for the expenses incurred by the winner and if the court does decide to do otherwise, they are mandated by the statute to furnish their reasons for the same. India is in a unique situation where although they do follow the loser-pays principle in an effort to ward off false and vexatious claims, in reality the costs decided by the court is minimal compared to the value of the suit such that it does not pose as a barrier or in other cases, no costs are levied on the loser of the suit at all.[15]

Along with the rise of TPLF, the emergence of Legal expenses insurance (LEI) has also provided a new dynamic in the legal market. Legal expenses insurance is of two types: (i) Before-the-event insurance (BTE) (ii) After-the-event-insurance (ATE). BTE is the type of insurance that is widely known by the general consumer and which can be procured for commodities like car insurance, house insurance, life insurance, etc.[16] The Ministry of Justice of England and Wales recommended that Legal expenses insurance should be extended to include employer provision to employees and housing association provision to tenants. However, research by Citizens Advice (Previously known as Consumer Focus) showed that only 48 percent had successfully used LEI and the majority were unsatisfied with the product.[17] On the other hand, ATE is a type of insurance that covers against the liability for adverse costs in the event that a suit is lost and the onus of paying the litigation costs of the winning party is thrust upon the claimant. ATE is gaining prevalence in common law countries like the U.K., U.S. and most civil law countries. ATE can usually be availed at any time before the trial's concludes. The claimant pays a premium, which largely depends on the facts and circumstances of the particular claim and the insurer. The premium does not have to be paid if the case is lost, but only payable if it is successful. ATE essentially amounts to the funder attempting to hedge their bets as otherwise, the burden of paying adverse costs in the event that the suit is unsuccessful can cause the funder to face greater losses overall.[18] Although not as widely prevalent in India like in Western countries, LEI of the BTE kind can be purchased just as easily as purchasing any other kind of insurance policy.

Every jurisdiction has rules that regulate the economic consequences of litigation, i.e. rules

14 Code of Civil Procedure, 1908 (5 of 1908), s.35
15 *Supra* note 18 .
16 Cento Veljanovski, *"Third Party Litigation Funding in Europe"*, J.L. ECON. & POL 405 (2012).
17 Hodges, John Peysner, *et.al.*, *"Litigation funding: status and issues."* (2012). Available at: *https://www.law.ox.ac.uk/sites/files/oxlaw/litigation_funding_here_1_0.pdf* (Last visited on March 25,2021).
18 *Supra* note 21.

on litigation costs. The basic elements that make up quantifiable costs are the same in every jurisdiction. There are composed of three elements:

a. Charges for use of the courts and their processes, including associated officers and bailiffs;

b. Evidential costs for witnesses and experts;

c. Lawyers' fees, where lawyers are involved,

d. Cost of appointing and hiring arbitrators (In Arbitration)[19]

Although, legal systems across the world vary widely in their processes and in economic terms, there are, however, paradigms that all legal systems intrinsically possess. Courts always levy charges for the use of the courts, including any personnel e.g. officers and bailiffs. These charges can vary in amount, ranging from nominal costs in France to quite high prices like in the U.S. and Singapore. There also exists costs pertaining to the procurement and transportation costs for witnesses and experts in general. Lastly, lawyers' fees are an indivisible part of the legal system and although the structure of the fee payment can vary widely from an hourly-basis or a flat fee, to a contingency fee based on the success of the case.[20]

For large commercial cases between multi-national entities, International commercial arbitration is emerging as the premier method of adjudicating matters primarily due to factors such as confidentiality, choice of panel/institution, customised procedure, etc. The International chamber of commerce in 2016 adopted a 'Guidance note for the disclosure of conflicts by arbitrators' which contained a reference to Third-party funding. The note 'states that an arbitrator ought to consider whether to make a disclosure if there exists relationships with any entity having direct economic interest in the dispute or an obligation to indemnify a party for the award.' Hence, if the arbitrator and the funder happen to have a direct or indirect relationship between each other, the arbitrator ought to notify the opposing party such that both parties and the arbitrator can come to a conclusion as to what must be done subsequently. The development of international arbitration and India as an arbitration hub is negligible in comparison to the Singapore International Arbitration Centre (as evidenced by the 485 cases concerning Indian parties arbitrated in the SIAC) but is likely to grow in the coming years.[21]The factors holding back the progress of arbitration in India largely comes

19 *Supra* note 12.
20 *Supra* note 12.
21 Available at: https://www.siac.org.sg/images/stories/articles/annual_report/SIAC%20Annual%20Report%202019%20(FINAL).pdf (Last visited on March 30, 2021)

down to the costs associated with arbitration (i.e. Arbitrators' fees, legal fees, fees of the arbitral tribunal, travel and other expenses of the arbitrators, administrative fees, etc.) and the general confidence in the competence of the existing judicial system. Furthermore, the lack of staying power is concerning wherein the order of the arbitration can be challenged on certain grounds as laid out in section 34 of the Arbitration and Conciliation Act, 1996 and this just serves to elongate the process of claim compensation. Singapore[22] has emerged as a beacon for arbitration in the Asian-pacific region and is also the first Asian jurisdiction to recognise Third-party funding in international commercial arbitration.[23] It would be pertinent to mention that, although there are provisions for legal aid empowered by the Constitution of India, there are no similar provisions in the Arbitration Act for cash-strapped organizations. Hence, the inclusion of TPLF in arbitration regulations could be seen as a first step to test the waters of TPLF in India and to enhance the attractiveness of India as a potential International arbitration hub.[24]

In order to determine who is the 'owner' of a particular claim, it is important for the existence of a TPLF agreement to be disclosed at the outset of the arbitration. Currently, there is no obligation on the party to disclose a TPLF agreement. Several countries, who have accepted the use of TPLF practises, have made it mandatory to disclose the existence of a TPLF agreement. However, these mandates are only of a persuasive nature and are not legally binding on the parties.[25]

II. TPLF IN OTHER COUNTRIES

(A) United States

The present scenario of TPLF in the U.S. is that a small number of companies provide funding to large corporates who prefer not risk their own assets and rather use their capital in the day to day running of their business. Juridica Capital management Ltd., is the largest firm operating in the U.S. and primarily invests in large commercial claims (Antitrust, Intellectual Property, commercial contract breach, etc.). It usually invests around $3 - $10 Million into claims of value of at least $25-100 Million. Another behemoth in the TPLF industry is Burford Capital Limited, who provides support for significant corporate litigation, arbitration and other disputes.[26] Funders in the U.S. are adamant on only working with claimants who

22 Civil Law Act (1999) (Sing.), Civil Law (Third-Party Funding) Regulations (2017).
23 Ridhima Sharma, *"Third Party Funding in International Commercial Arbitration"*, 12 NUALS L.J. 61 (2018).
24 *Supra* note 14.
25 *Supra* note 3.
26 *Supra* note 9.

have hired lawyers on a contingency fee basis, as this adequately aligns the interests of the legal counsel, the claimants and the funders in achieving a successful outcome. The remuneration received from the final award is split between the lawyers and the funders based on prior agreements and the remaining amount is left with the claimant.[27] The American courts have rarely enforced the doctrines of champerty to void TPLF agreements.[28] Some jurisdictions have gone so far as to abolish the doctrine of maintenance and champerty on the grounds that it does not protect against the institution of frivolous lawsuits,[29] and other public policy concerns could be addressed more efficiently by other means.[30] Interestingly, one of the hallmarks of the U.S. legal system is the absence of a loser-pays rule (cost-shifting) in effect; this could be one of the causes of the propensity of American citizens and entities to pursue litigation, making it the capital of Tort litigation in the world.

(B) United Kingdom

In addition to the funding of large commercial litigation, the U.K. demonstrates that TPLF can cover such areas such as personal injury and family matters. Private litigation funding is the by-product of public policy trends during the 1980's and 1990's that reduced the ease of access to legal aid on the grounds that it was too expensive and endorsements were given to private funding practices which were rationalised as access to justice. The new policy directive shifted the funding of claims relating to physical or mental injuries to the private sector.[31] Companies operating in the UK litigation funding market include IM Litigation Funding, Harbour Litigation Funding Ltd., and Juridica Investment Limited. While these companies could, until recently, be characterized as "alternative investment firms".[32] *Arkin v. Borchard Lines*[33] was the landmark judgement that intimated that third-party funding should not only be tolerated but also encouraged as a useful tool for facilitating access to justice. Another milestone in the roadmap for TPLF in the U.K. was the report published in 2010 by Justice Jackson in what is now famously called the Jackson reforms wherein Hon. Justice Jackson went on to state that 'in some areas of civil litigation, the costs are disproportionate and impede access to justice'.[34] In order to increase the access to justice, Justice Jackson stated that third-party funding is beneficial and should be supported.[35]Although, the Jackson

27 *Supra* note 4.
28 Gowen v. Helly Nahmad Gallery, Inc. (2018) 77 N.Y.S.3d 605 (N.Y. Sup. Ct.)
29 Robert Bone, "*Modeling frivolous suits*" University of Pennsylvania Law Review 145.3, 519-605 (1997).
30 *Supra* note 9.
31 *Supra* note 12.
32 *Supra* note 9.
33 *Arkin v. Borchard Lines Ltd.*, (2005) 2 Lloyd's Rep. 187 (Eng.).
34 Rupert M. Jackson, "*Review of civil litigation costs*", The Stationery Office,(2010).
35 *Supra* note 9.

reforms provide a framework for viewing third-party funding, there yet does not exist any regulation for third-party funding and the firms who practise it and the field thus far has been largely self-regulated.[36]

(C) Australia

Australia as a common law country has practices similar to that of England and they also employ the cost-shifting rule (The cost-shifting rule allows the winner of the litigation to recover its litigation costs from the loser). However, it has been observed that successful litigants will not be able to shift the entire cost of the proceedings onto the loser and the usual ranges of these estimates are between 30 to 50 per cent.[37] Presently, legislation in the Australian Capital Territory, New South Wales, South Australia and Victoria has expressly abolished maintenance and champerty both as a crime and as a tort. It is still, however, at the discretion of the court that they may set aside a TPLF agreement if it is found to be inconsistent with public policy considerations upon which the prohibition was based on common law, alike the stand that the U.K. and Indian courts have taken.[38] The Australian judicial system is regulated by state territory law; these laws require law firms to provide their clients estimates of the costs of the case. These costs consist of the hourly rate and other miscellaneous expenses. Some law firms are moving away from this model in favour of a fixed fee model for specific tasks that the amount of man hours necessary for its completion can be estimated somewhat accurately (e.g. Preparation of a will or contract). Another common billing arrangement is the conditional fee wherein the lawyer will not be paid until the case is resolved, if it is successful the lawyer will be paid his hourly rate with a percentage increase, usually up to 100 per cent increase, and if it is unsuccessful the lawyer will not be paid at all. This is different from the contingency fee model, which is prohibited in Australia, wherein the lawyer is entitled to a percentage of the claim the claimant receives from the final award. Commercial litigation funders exist and thrive in Australia primarily because of the costs shifting rule and the prohibition against lawyers charging contingency fees. Similar to the U.K., as of yet, there exists no regulation tailored to the nature and execution of third-party funding and is largely self-regulated by individual funding firms.[39]

It was first in the case of *Campbells Cash & Carry Ltd. v. Fostif Pty. Ltd*.[40] where the Australian High Court gave its approval for litigation funding. Since then, other judges have

36 Camille Cameron and Jasminka Kalajdzic. *"Commercial Litigation Funding: Ethical, Regulatory and Comparative Perspectives."*, Can. Bus. LJ 55 (2014).
37 VLRC Civil Justice Review 681-693 (2008).
38 *Supra* note 12.
39 *Supra* note 12.
40 (2006) HCA 42.

also endorsed the merits of commercial litigation financing for its potential to improve the efficiency and accuracy of litigation.[41] In *International litigation partners pte Ltd. v. Chameleon Mining*[42] the court mulled over whether TPLF agreements constituted a financial product under the corporations act, and if so, the funder must hold an Australian Financial services License to continue operations. By a 2-1 majority, the New South Wales court of appeal held that litigation funding did constitute as a financial product according to the statutory criteria because it managed risk in relation to costs and claims and therefore it required an Australian Financial services License. Subsequently, after the judgement any funders operating in the litigation finance industry must hold a financial services licence.[43] The requirement to hold a Financial Services Licence carries with it a number of obligations under the Corporations Act.[44]

(D) Canada

The Canadian Legal system can be seen to have incorporated legal ideas from both their Australian and U.S. counterparts, wherein the costs of litigation is redistributed by the court at the end of the litigation by means of cost-shifting. It also borrows the principle of contingency fees from the US which permits lawyers' fees to be tied to the success of the particular client's case.[45]The TPLF market in Canada, similar to the U.S., is only a few decades old and has largely only been seen in the context of class-action suits. And unlike in Australia, Canadian courts have been adamant that funder's cannot have a contractual right to exercise any control of the decision-making and conduct of the litigation.[46] Funding in litigation is still burgeoning in both the United States and Canada, but appears to be more active in Canada, where the need for indemnities against adverse cost awards has created a market demand for funders that does not exist in the United States.[47]

(E) France

The industry of TPLF has so far failed to catch on in France, which could be largely due to internal factors such as nominal court costs and widespread availability of legal aid. Furthermore, costs of proceedings are usually easily available and so it is easier to budget for legal costs. Loans or grants from banks or other entities are allowed for the pursuit of

41 *Supra* note 9.
42 (2011) 276 ALR 138.
43 Available at: *https://asic.gov.au/regulatory-resources/funds-management/litigation-funding/#afs*
44 Corporations Act of 2001 s 912A (d). as cited in (George R. Barker, *"Third-Party Litigation Funding in Australia and Europe*", 8 J.L.), ECON. & POL'y 451 (2012).
45 *Supra* note 12.
46 Jasminka Kalajdzic, *"Self-Interest, Public Interest and the Interests of the Absent Client: Legal Ethics and Class Action Praxis"* OSGOODE HALL L.J. 49 (2011).
47 *Supra* note 5 at 93-148.

litigation under French law but are not used in practise.[48]

(F) Germany

The German legal system is marked by its high predictability of litigation costs.[49] Nevertheless, for highly complex cases it would be difficult to find a lawyer/firm that is prepared to accept the workload merely on the remuneration as prescribed by the statutes. Cases that require extensive gathering of information, experts and witnesses would also see a proportionate increase in the resulting litigation costs. TPLF, although a growing industry in Germany, a large number of the German population possess legal expenses insurance and as a result, TPLF is only restricted to large commercial claims. The proliferation of legal expenses insurance in Germany is in large part due to the aforementioned predictability associated with the German legal system.[50]

(G) Netherlands

The Netherlands has a history of alternate dispute resolutions systems such as dispute resolution boards, arbitration centres and ombudsman-like institutions. The most popular by far is the dispute resolution board which aims to resolve disputes between consumers and a professional/organization. Nominal fees are only charged for its use and the ruling of the dispute resolution board is issued within a few months and can be enforced with the assistance of traditional courts.[51] The market of TPLF is present in the Netherlands but has not taken off on a wide scale. However, famously in 1997 a claim was funded by means of being publicly traded on the Amsterdam stock exchange.[52] The claim was regarding the prosecution of a Dutch businessman and his company and he subsequently claimed compensation from the state for the damage caused to his reputation. The claim was de-listed from the stock market once the courts ruled unfavourably.[53]

(H) Switzerland

Other than the prohibition for contingency fee systems, no law explicitly forbids the practise of TPLF in Switzerland. Allianz ProzessFinanz, a subsidiary of Allianz Inc., is its ligation finance wing and is a large player in litigation funding in Switzerland. The firm only supports claims over CHF 300,000 and covers lawyers' fees, court fees, and cost for experts and any

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48 *Supra* note 12.
49 'Law–Made in Germany', 29 the booklet is available at *www.lawmadeingermany.de* (Last visited on 21 March, 2021). As cited in *Supra* note 10.
50 *Supra* note 12.
51 *Supra* note 12.
52 Volkskrant, "*Flitsende start van Begaclaim op Amsterdamse effectenbeurs"*(1997), As cited in Supra note 11.
53 *Supra* note 12.

other dispute related expenses. Allianz's share of the proceeds is 30 per cent and if the case is settled within the first 6 months, its share is reduced to 20 percent.[54]

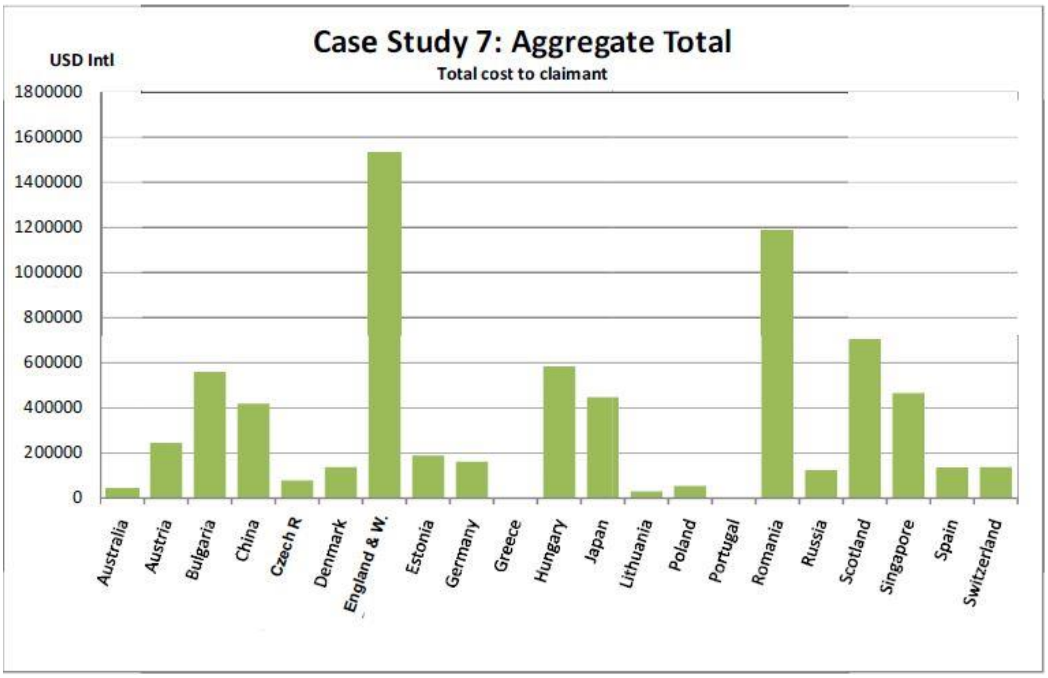
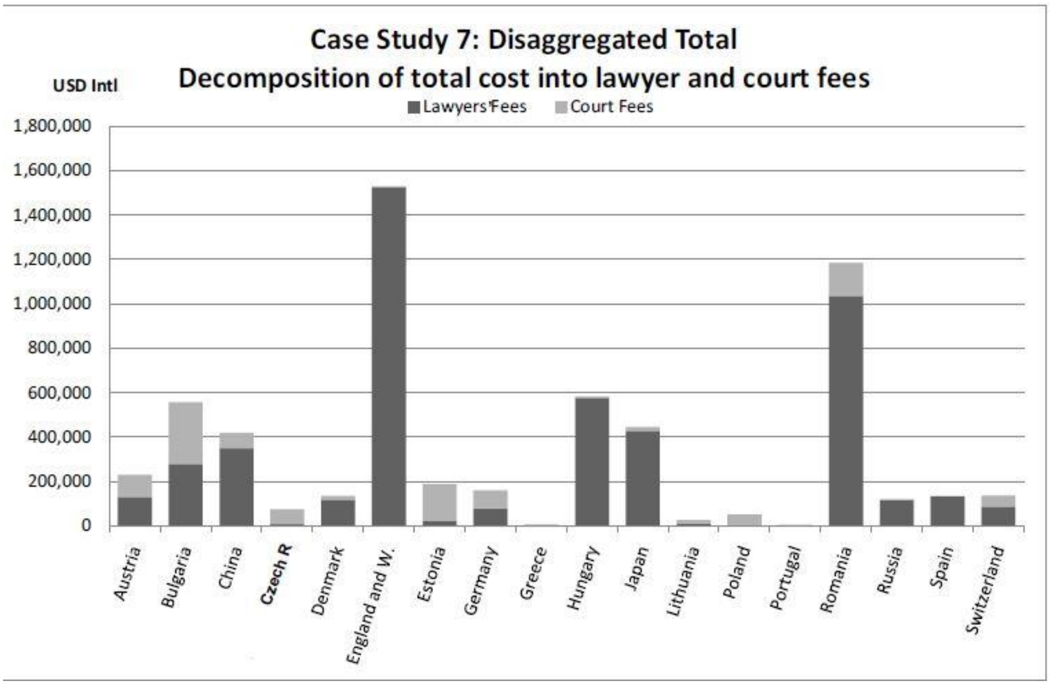


Figure 1.1 - Case study 7: Represents a Large commercial case scenario wherein a substantial and complex breach of contract claim between two large companies over supply of defective machinery worth €2 million, with €5 million loss of profit. As found in Hodges, Christopher, Stefan Vogenauer et.al, "The costs and funding of civil litigation: a comparative perspective", Bloomsbury Publishing, (2010).



54 *Supra* note 12.

Figure 1.2, A decomposed representation of figure 1.1 as found in Hodges, Christopher, Stefan Vogenauer et.al, "The costs and funding of civil litigation: a comparative perspective", Bloomsbury Publishing, (2010).

The graphs above[55] can be surmised into the following findings:

- The total cost of litigation varies widely between countries and is not uniform even for the same type of claim.
- Lawyers' fees constitute the majority portion of the costs associated to litigation and although in some jurisdictions court fees are higher than in others, the court fees represent only a small percentage of the total litigation costs.
- Court costs are largely predictable owing to the propensity for legal systems to encode them and pass them as law. This is even more prevalent in civil law countries but common law countries, by and large, follow this practise as well.
- Lawyers' fees are largely unpredictable but are usually proportional to the complexity of the particular claim across jurisdictions.
- In most jurisdictions the costs of litigation are high in relation to the value of the case. Sometimes costs can even exceed the value of the case if the claim is not for a large amount and hence pursuing a claim through the civil court system was not the recommended or most popular route for obtaining redress in the given situation, and that alternative solutions are preferred.[56]

III. Challenges facing TPLF in India

Jurists and academics who have acted as a buttress for TPLF claim that the industry is vital for closing the gap between plaintiffs and defendants, the former who is usually but not always of a weaker standing financially.[57] In addition, claimants who can rely on a ceaseless flow of funds need not buckle to accept any low settlement offers. The funder also has a personal duty to perform their due diligence processes before agreeing to fund a particular claim as their business model is primed on taking calculated risks by agreeing to fund a legal claim wherein the result, although can be approximated by legal experts of that field, is never predictable. It would not be a stretch to state that parties contemplating to knowingly breach a contract or commit a legal wrong will think twice if the victims are able to count on solid

55 *Supra* note 12.
56 *Supra* note 12.
57 *Supra* note 9.

financial resources through TPLF.[58]

The critics who are vehemently against TPLF argue that the inclusion of a third party who was not part of the initial breach/claim can lead to a conflict of interest. TPLF can also exert undue influence on courts as their presence provides a veil of sustainability for the claim in the eyes of the court as an externally funded claim would by the very fact that it would have gone through the stringent due diligence process of the funder, very well could be perceived to have more merit than an internally funded claim. Furthermore, arbitrators could have a direct or non-direct link to the funder which could cause a conflict of interest if not disclosed. The increased access to TPLF could also cause claimants to be taken advantage of, especially in cases where the claimant does not have much technical expertise in the matter. The claimant could be coerced into agreeing to a funding agreement that does not serve his best interest. It can also be argued that the advent of TPLF in the Indian legal system will cause the already back-logged courts to be flooded with even more frivolous suits instituted off the back of TPLF.[59]

If there was one obstacle that could be accredited with causing the scepticism with respect to TPLF it would have to be the doctrine of champerty which can be defined as “an agreement between an officious inter-meddler in a lawsuit and a litigant which the inter-meddler helps pursue the litigant's claim in exchange for receiving a part of any judgment proceeds.” Although many common law jurisdictions have abolished or relaxed the use of the doctrine in support of TPLF, champerty still serves as a rule of public policy that can render a funding agreement void and unenforceable. There has been an undeniable amount of change in trade and law which justifies the loosening of its severity and allowing TPLF to develop.

Usury also seems that it can pose a threat to the operations of TPLF and the validity of funding agreements. Usury can be defined as the charging of interest at a rate in excess of that allowed by law. The elements necessary for a usurious transaction are: (1) a loan of a sum of money; (2) an absolute obligation to pay the principal; (3) extraction of compensation greater than what is allowed by law from the borrower. It is for these reasons, TPLF firms have taken the position that their actions are not usurious and against the law as they do not provide regular loans and the financing they provide is non-recourse in nature.[60] The funding agreement is more akin to a purchase of a part of the proceeds of a claim and not a loan

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58 *Ibid.*

59 *Ibid.*

60 Yifat Shaltiel, John Cofresi, *“Litigation Lending for Personal Needs Act: A Regulatory Framework to Legitimize Third Party Litigation Finance”*, 58 CONSUMER FmN. L.Q. REP. 347, 348 (2004).
(2004). as cited in *Supra* note 7.

which would be subject to laws prohibiting usury.[61]

Attorney-client privilege poses an ethical dilemma for attorneys wherein they have to juggle between the confidentiality that exists between them and the client while also providing as much information as possible to the funders. Usually for these reasons, anything that is not public knowledge can only be disclosed to the funder via the attorney if the client agrees to waive his right to confidentiality. Juridica Capital Management Ltd., a TPLF, emphasized in its comments that "an analogy to a potential funding transaction is a potential merger between companies. As like a potential merger partner, a prospective funder has an interest in clarifying the strength of any legal claims or defences of the potential litigant in order to decide whether to proceed with the transaction”.[62]Considering this, it does not seem to be to invasive of the client’s rights in order for the funder to make the best decision possible. Establishing the counsel for the TPLF as the agents of the client is an option to bypass the right to confidentiality in order to conduct adequate case evaluation.[63]

It is not always necessary that the claimant and the funder will be on the same page with respect to what constitutes as a reasonable settlement offer. For example, a claimant might be inclined to accept a low settlement offer as he seeks to resolve the conflict as soon as possible but this might not be in the best interest of the funder as the low amount might not be enough for them to sufficiently profit from the transaction. It is also entirely possible that a TPLF would push for a swift settlement for a moderate sum, as this would allow the funder to keep the litigation costs low and increase his profits while on the other hand, the claimant, who does not have to pay for the litigation expenses, would rather continue to pursue the matter against the opponent. In a scenario where the settlement offer is made in assets rather than in cash, the TPLF might be more reluctant to accept the offer than the claimant as it would take more time to recoup their investment. In each of these cases, depending on the agreement between them, the TPLF and the claimant would come to a conclusion either by mutual deliberation or by enlisting the expertise of an external counsel.[64]

While in India, TPLF faces a different set of challenges. Firstly Class-action suits, which are the primary source of exemplary damages that attracts TPLF in the U.S. and Australia, are still in the nascent stage and have not gained much traction as of yet in India. Secondly, Indian courts are more averse to awarding exemplary damages for commercial disputes and

61 *Supra* note 7.
62 *United States v. Gulf Oil Corp* (1985) 760 F.2d 292 (D. Alaska) as cited in *Supra* note 7.
63 *Supra* note 7.
64 Vicki Waye, *"Conflicts of interests between claimholders, lawyers and litigation entrepreneurs."* Bond L. Rev. 19 (2007).

personal injury cases. The prohibition of the contingency fee model puts the entire litigating cost burden on the funder and is thereby harder to align the interest of the legal counsel to the success of that particular matter.[65]

IV. LEGAL BARRIERS FOR TPLF IN INDIA

So far, the development of TPLF in India has largely been negligible and only recently with the launch of LegalPay[66] in January of 2020, the first Third-party litigation funding firm in India, has there been any growth in this field in the Indian sub-continent. Though not prohibited by any Indian laws, the development of the TPLF market has been hindered by the public policy principles of maintenance and champerty, vestigial doctrines that remain from the British era. However, the Supreme court[67] has held that the strict interpretation of maintenance and champerty are not applicable in India and are not violate of public policy per se.[68] It ought to be taken into consideration that the country that created these public policy doctrines have since abolished their use in a strict application.[69]

In India, champertous agreements are only considered illegal if advocates are involved as decided in *Dr. V.A Babu Legal v. State of Kerala.*[70] Agreements that are unreasonable or unjust to the other party or that have an insidious motive behind it like that of gambling in litigation or in order to oppress another party are considered to be champertous. In order to differentiate TPLF agreements from an ordinary wagering agreement, the nature of a contingent contract first must be defined. A contingent contract is one where parties agree to do certain things based on the happening or non-happening of a particular event. The main difference between a wagering agreement and a contingent contract is that the parties have a personal interest in the occurrence of the event and not merely an interest in the event for the reason of the execution of the contingent contract. Furthermore, the events defined in contingent contracts are not a game of chance but based on calculation and risk assessment, which is the backbone of the due diligence process associated with TPLF. A wager, on the other hand, is a promise to pay money or money's worth on the happening or non-happening of an uncertain event. The parties do not have any personal interest in the subject matter of the event but only in its outcome in relation to the wagering agreement. Wagering agreements are considered void as per Indian law and illegal in some states such as Gujarat and

65 Available at: *http://www.cyrilshroff.com/wp-content/uploads/2019/06/Third-Party-Funding-in-India.pdf* (Last visited on March 21, 2021).
66 Website available at: *https://legalpay.in/* (Last visited on March 28, 2021)
67 *Bar Council of India v. A.K. Balaji* (2018) 5 S.C.C. 379
68 *Mr 'G' A Senior Advocate v. Unknown* (1955) 1 S.C.R. 490
69 *Supra* note 14.
70 CRP. No. 933 of 2002 (E).

Maharashtra.[71]

Another impediment to TPLF could be the time it takes for a case to be disposed of and an award to be granted to a party. Indian courts are infamous for having cases that drag on for generations. In a study conducted on 2 million cases that were filed between 2010 and 2016, it was found that it took an average of 15 months for a case to be disposed.[72] This seems to be encouraging for TPLF firms, however, it must be noted that these cases included cases of all types and not the particular type of cases that TPLF firms would usually invest in, so a slim inference can only be drawn from the data.

Fundamentally, the question of the legality of a TPLF agreement in India will come down to the issue of true control of the process of litigation. In countries, where the rules of maintenance and champerty do not apply, legal claims may be sold and bought as securities much like stocks and the funder may keep complete control over the assignment of the case ranging from the selection of particular legal counsels to running the day to day management of the claim. In countries where the ban on maintenance remains, like India, the funder must cede control to the original claimant and only can express opinions on the matter but the final decision must be left in the hands of the claimant.[73]

A sector where the assistance of TPLF could prove useful is disputes relating to breach of contract especially in engineering procurement contracts (EPC). Undoubtedly, the number of disputes would have risen owing to the global lock-down during 2020 which would have resulted in missed deadlines and a breach of the EPC. Regardless of nation-wide lock-downs, EPC face breaches regularly due to supply chain disruptions, shortage of materials or labour strikes. Hindustan Construction company Ltd. Was the first EPC Company to monetise their legal claims with investors led by Blackrock Inc.. Hindustan construction sold their claim for 1,750 crores but the potential value of the claim is upwards of 4000 crores.[74] This early example exhibits the latent possibilities for cash-strapped companies and TPLF firms.

In the case of *Union of India v. A.K Balaji*[75], the Supreme Court 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." This seems to clarify the Apex courts' position on the legality and permissibility of TPLF in India.

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71 Ridhima Sharma, *"Third Party Funding in International Commercial Arbitration"*, 12 NUALS, L.J. 61 (2018).
72 Available at: *https://dakshindia.org/leading-indicator-case-duration/* (Last visited on 21 March, 2021)
73 *Supra* note 22.
74 *Available at: https://in.reuters.com/article/hindustan-constr-debt/indias-hindustan-construction-to-move-awardsclaims-to-blackrock-led-investors-idINL3N21D23A* (Last visited on: March 21, 2021).
75 *Bar Council of India v. A.K. Balaji* (2018) 5 S.C.C. 379

Section 23 of the Indian contract act goes on to state that the consideration and object of a contract is lawful, unless it is either forbidden by law, considered immoral in the eyes of the court or is opposed to public policy. With the doctrines of maintenance and champerty still in place, it is essential for TPLF agreements to not seem overambitious in extracting a high percentage of the award, lest it be deemed by the court to be immoral or against public policy.[76]

V. FORMULA FOR CLAIM EVALUATION

As we can imagine, funders would not be interested to invest in every litigation claim that comes their way and as discussed before, a strenuous due diligence process must be conducted especially as the numbers involved in large commercial cases are high. A funder will only look to invest in a claim if the likelihood of turning a profit is higher than the cost to fund the claim. Fundamentally, this can be represented in the formula, where $E(c)$ represents expected cost of funding the claim, $E(r)$ represents the expected total revenue the claim generates, S represents the probability that the claim is successful and $E(\mu)$ represents the expected profit that arises from the claim.

$$E(\mu) = S*E(r) - E(c)$$

The funder, whose aim is to maximise profits, will only fund claims where the expected revenue generated from funding the suit is greater than the expected costs.

We know that the majority of funders take only a percentage of the proceeds from the claim, which would be a multiple of the amount they would have invested in it initially. Let σ be the percentage of the claim that is owed to the funder, R be the total revenue generated from the claim.[77]

So, $E(r) = \sigma*R$

We get, $E(\mu) = S*\sigma*R - E(c)$

If any claim is to be invested, it must satisfy the formula such that $E(\mu) > 0$.

Exploring the formula with an example, assuming that R= INR 1,00,00,000; S= 80%; σ =35%; E(c) = 10,00,000 Rupees.

Here, $E(\mu)= 0.8*0.35*1{,}00{,}00{,}000 - 10{,}00{,}000$

$E(\mu) = 28{,}00{,}000 - 10{,}00{,}000$

$E(\mu) = 18{,}00{,}000 > 0$

76 The Indian Contract Act, 1872 (9 of 1872), s. 23
77 *Supra* note 9.

So, it would make economic sense for a funder to invest in this claim.

Let us take another example where, R= INR 10,00,00,000; S= 40%; σ = 35%; E(c) = 50,00,000 Rupees.

Here, $E(\mu)= 0.4*0.35*10{,}00{,}00{,}000 – 50{,}00{,}000$

$E(\mu) = 1{,}40{,}00{,}000 – 50{,}00{,}000$

$E(\mu) = 90{,}00{,}000 > 0$

It seems from a purely analytical perspective; funding claims that can generate much higher revenues but have a lower probability would be more lucrative than funding claims with a higher probability of success but with a lower pay-out. Furthermore, TPLF firms are in a position where they can diversify their portfolio with high value-low probability claims and low value-high probability claims, which would allow them to absorb losses on low chance of success cases as compared to other financial institutions or a high net-worth individual.

Another point of interest is what are the factors that determine whether a case is deemed to have a high probability of success? Although, it would be unwise to place definite values on certain factors, we can list some of the possible factors and determine whether they would decrease the probability of success (-) or increase the probability of success (+).

Some factors which would determine how likely a funder would be to invest in a claim are:

- Documentary evidence showcasing the liability of the defendant to pay damages (+)
- Claimant who has previous experience in litigating suits of similar subject matter (+)
- Unambiguous judicial precedent in favour of the claimant (+)
- Defendant with deep pockets usually have a willingness to come to a settlement (+)
- Hiring of lawyers lacking expertise or experience in the particular field of law (-)
- If the suit is primarily based on the testimony of witnesses (-)
- If the claimant is pursuing the suit for malicious and not pecuniary reasons (-)
- If the presiding judge over the matter has a track record of favouring the defendant/other party in suits of the nature (-)

VI. Viability of TPLF in India

From a business perspective, there is hardly any difference between other avenues of investment and TPLF which would justify its prohibition on moral or ethical grounds. It provides an opportunity for claim holders to manage litigation risk and monetise their claim.

Both parties are made better off by agreeing to a TPLF agreement as the claimant eliminates the risk of an unfavourable outcome while the funder procures an opportunity to multiply the amount he invested in the claim.[78]TPLF firms need not reinvent the wheel when creating and operating their firms as the economics of venture capitalism (VC) are quite similar to the world of litigation finance. Both institutions are distinguished by their (1) uncertainty; (2) information asymmetry; (3) agency costs.

Both venture capitalists and TPLF firms manage portfolios or high risk- high return entities. Venture capitalism is the practise of investing in companies that specialise in cutting-edge and esoteric products.[79] They face the same form of information asymmetry wherein the entrepreneurs running the company know much more about the technology than the VC and no amount of external expertise would be able to adequately bridge the gap of knowledge between the entrepreneurs and the VC. Similarly, the claimant who approaches a TPLF firm for funding has more information about the particular history of the claim than what might be made available to the funder. Furthermore, some claimants might think that it is in their best interest to consciously hide certain information or the existence of potentially harmful witnesses or evidence from the firm in order to procure funding. TPLF firms also face the extra-legal barrier of attorney-client privilege before they are able to attain the necessary information.[80]

Litigation financiers in addition to the uncertainty and information asymmetry, face the uncertainty and costs caused by the dependence on agency (lawyers and the plaintiff) to perform their duties. If the plaintiff, for whatever reason, loses interest in the litigation especially as now they do not have to bear the costs of the litigation, this can pose a significant threat to the success of the suit. Although not to the same extent as litigation financiers, VC also face the same problems as mentioned above and it would be beneficial to adapt solutions from the established theory, contracting and practise of Venture capitalists. Organizationally, the TPLF firm would be best suited to operate as a limited partnership[81], where the general partner is a company comprised of investment and legal experts and the investors providing the resources for investing into claims and for the operation of the firm are passive limited partners. These passive limited partners who do not participate in the day to day running of the firm would most likely be a private equity firm or a high net-worth

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78 *Supra* note 9.
79 Ronald J. Gilson, *"Engineering a Venture Capital Market: Lessons from the American Experience"*, 55 STAN. L. REv. 1067, 1069 (2003). as cited in Maya Steinitz, *"The Litigation Finance Contract"*, 54 WM. & MARY L. REV. 455 (2012).
80 Maya Steinitz, *"The Litigation Finance Contract"*, 54 WM. & MARY L. REV. 455 (2012).
81 *Supra* note 84.

individual (HNI) looking to diversify their portfolio into alternate investment classes.[82]

The general partners, who are in charge of the operations of the firm and deciding what claims are worthy of investing into, would receive compensation which is usually around 20 percent of the realised profits which is the norm in private equity firms.[83] A 2% of the total assets of the firm are usually demarcated as a yearly management fee which would be used for day to day operations. The majority of the general partners' duties consist of making non-cash contributions such as case management and playing a role in shaping the strategy of the litigation of each invested claim.[84]The funder can also assist the plaintiff in formulating settlement agreements. Furthermore, the presence of a funder is a signalling mechanism to the court and to the opposing party that the claim in question is of such merit that an objective third party deemed it meritorious enough to invest in the claim. This can lead to early settlements or at the very least will result in the court not dismissing the suit at the outset. In the same vein, if it is known that the plaintiff has sought litigation financing but has failed to receive it, it would decrease the virtue of the claim in the eyes of the court.[85]To benefit from the general partners' knowledge and expertise in the field, the passive partners must allow them to hold a disproportionate control over the running of the firm. This agency problem can be solved by fixing a term by which it would be easily observable if the general partners' have been successful in their pursuits thus far and whether their track record warrants additional funds from the same or other investors. In the world of venture capitalists, this problem is solved by conducting the financing through stages.[86] The first round investors are not obligated to participate in future rounds, additionally, the general partners are also permitted to seek investment from other sources. Staged financing can similarly be done in the context of third party funding to align the interests of the general partners to the interests of the passive partners (investors).[87]

TPLF like any other asset class, is a high potential but risky financial product that requires extensive due diligence, poses a high barrier to entry, is not scalable and is generally illiquid. The collection of recoveries is not a straightforward process and the firm would have to spend resources and time towards that effect. The success of a TPLF firm also largely revolves around its ability to network effectively. The majority of claims are usually referred to TPLF firms by lawyers and a good standing among the biggest law firms in the

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82 *Supra* note 85.
83 *Supra* note 84.
84 *Supra* note 85.
85 *Supra* note 8.
86 *Supra* note 84.
87 *Supra* note 85.

state/country is essential for the continued performance of the TPLF firm.

A noteworthy point when constructing a TPLF agreement, is what percentage of the proceeds can be assigned to the funder such that the contract will not be considered extortionate and against public policy.[88]In the U.K., the percentage typically ranges from 20% to 40% of the proceeds of the settlement. In Austria, Germany, Ireland, and the Netherlands, the experience is similar, a success fee from 20% to 40%. These ranges are lower than in Australia, where TPLF investors' success fees range from 30% to 60%. In India, any percentage exceeding 40% is in danger of being considered as extortionate.[89]

The final part of this sub-section will deal with the essential rights that the funder needs to outline in the TPLF agreement. As mentioned before, attorney-client privilege needs to be waived in order for the funder to receive the same information on a case as the plaintiff/claimant. The funder should be able to express his opinion and outline legal tactics or strategies that the plaintiff may incorporate but this ought not to be binding on him. The funder ought to be allowed to schedule meetings with the plaintiff and the plaintiff’s legal counsel routinely to keep up to date with how the claim is proceeding. Furthermore, the funder should inscribe into the TPLF agreement the unilateral right to terminate its funding. This would only be invoked when a certain piece of information or evidence has come into light that drastically reduces the probability of a successful litigation outcome. However, by doing so the funder forfeits the amount already exchanged and these need not be returned, the finer details of each agreement may vary. The funder also may institute a clause wherein they may withdraw from its funding duties if there is a change in the legal counsel done after the agreement was signed. Before doing so, the funder may express his lack of confidence in the latest hiring of the legal counsel which may result in the funder making use of his unilateral right of termination of the agreement.[90]

VII. CONCLUSION

The global pandemic in 2020 undoubtedly would have increased the demand for third-party litigation funding. Facing extreme financial constraints, companies are more cautious about spending on litigation. The pandemic has also increased the volume of legal disputes and has resulted in a large number of companies shutting down operations in lieu of increasing financial burdens. Investors, with the volatility of the markets fresh in their memories, will be looking for a new alternative asset class, one that would be unaffected by trends in the global

88 *Supra* note 21.
89 *Ibid.*
90 *Supra* note 22.

markets. Third-party litigation funding could prove to be just that.[91] Fundamentally, TPLF seeks to address the problem of how can companies manage and even turn the costs and risks of litigation to a source of income. In exchange for alleviating the risk from the litigation, the claimant parts with a portion of the award if the litigation has a favourable outcome. The acceptance of TPLF by the judicial system would in turn foster the creation of more TPLF firms which in turn would increase the competition within the industry resulting in better terms and conditions for the consumer. Furthermore, the use of financial instruments such as credit-default swaps with another financial institution which would entail the TPLF firm to make periodical payments in exchange for receiving a pay-off in the event that the litigation is unsuccessful, thereby allowing the TPLF firm to hedge against their investment and reduce their loss in the event the that the litigation has an unfavourable outcome. The institution of a legal framework, concerning the regulation and rules a TPLF firm must abide by would go a long way in legitimizing the business in the eyes of the general public.[92]

In essence, TPLF can be considered as a revolutionary tool for victims seeking justice, in the absence of the financial ability to do so. The unavailability of the contingency fee model in India has created a distinct need for an alternate source of litigation funding in the country.[93]Finally, it is after a comprehensive outlook on the industry, that the author considers that third-party litigation funding is here to stay in India and in the coming years it is likely we could see indigenous third-party funding firms come to the fore along with the proliferation of already established players in the industry set up Indian branches to claim their share of the litigation funding market in India.[94] The advent of third-party funding will encourage enforcement of the law and will remove the bargaining power from the hands of a few corporates and reinstate it back with the victims. This is the equality of power that businesses have long been anticipating.

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91 Maya Steinitz, *"Whose Claim is This Anyway-Third-Party Litigation Funding"*, 95 MINN. L. REV. 1268 (2011).
92 *Supra* note 9.
93 *Supra* note 5.
94 *Supra* note 14.