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for Legal Protection International (LPI) – https://legalprotectioninternational.com

Dear Antje,
dear Simon,
dear participants,

Thank you very much for the opportunity to have this exchange with you on the important topic of litigation funding!

Market and context

Let me first try to give you an overview of what this market is about. The markets reflect to some extent also different legal traditions: while we have a tradition in continental Europe of enforcing the public order via public law and authorities, it has been a strong tradition in common law countries, particularly in the US, to perceive court actions also as a means of enforcing rules of behavior driven by "private attorneys general", to have weaker public institutions but a strong means for private players to enforce the rules of the game. In continental Europe, collective compensation has rather been a supplement to public enforcement but not the primary means, not a substitute for public authorities in charge.

This general perspective on public and private enforcement may be at the foundation of the conspicuous observation we can make on **slide 2**: the big hubs for private commercial litigation funding are the US, the UK and Australia which seems to have seen the worst excesses considering the findings of the 422 pages report of December 2020 of the Parliamentary Joint Committee on Corporations and Financial Services on Litigation Funding and the Regulation of the Class Action Industry.

And **slide 2** also shows that this business is not about peanuts but about real money awaiting to be invested into litigation. The European Parliament's Research Service EPRS shows in its long study "Responsible private funding of litigation" of March 2021 that the top eight funders have command over a total capital for investment of € 7 billion, and there are several dozens more operating in Europe, may be an estimated close to 100 funders active, some 44 of them in the UK, 24 in the Netherlands, at least 13 in Germany with others operating in Austria, France, Spain, Portugal and Ireland. Litigation funding is even advertised as an asset class for investment which is not correlated to the usual movements of the capital markets.

As most funders are not companies who publish their figures, there are only limited opportunities to get information on returns. But the EPRS has collected information from various sources and come to the interesting conclusion that TPLF is even more profitable than investments into Hedge Funds or Private Equity, considering the multiples achieved on the capital invested basis, as we can see on **slide 3**. And if these figures are disputed by some you just need to point to the Submission the Funder Bentham made to the Dutch Ministry of Security and Justice on 14 October 2014 in their consultation regarding the Dutch Draft Bill on Redress of Mass Damages in a Collective Action, downloadable from the respective

consultation page: there, Bentham Europe reports on page 5 that IMF has "historically generated an average 298 % gross return on funds invested" a figure which is also quoted in the VOSS report.

Contents of the VOSS Report

(**Slide 4**) Now, such observations have led JURI MEP Axel VOSS of the EPP to raise the issue of a need to regulate the activity of Third Party Litigation Funding in the EU in order to protect EU citizens and companies to be unduly taken advantage of without any serious control. This is a legitimate impulse as extreme rates of return may point to situations of either market failure or even of public service failure.

If citizens' renunciation of violence is the correlate of the state's monopoly on the use of force, the state must also ensure effective enforcement of the law across all areas of law, possibly in proportion to the respective threat of harm, but in principle nevertheless in a way that does not severely restrict citizens and businesses by the rights to be guaranteed. Turning law enforcement into a business for profit, however, may lead to justice becoming the victim of conflicts of interests, i.e. between the interest of the funder to make as large and as quickly a profit as possible on the one hand and the interest of the beneficiary of the funding on the other hand to obtain full compensation of the damages owed to him or whatever else his objective may be – it certainly is not his objective to only be a tool for investment and not the actual main reason for bringing the respective action.

That is what the Draft Report 2020/2130(INL) by Axel VOSS with recommendations to the Commission on Responsible private funding of litigation to the Committee on Legal Affairs is about. Now, what are the main proposals offered to prevent private litigation funding of the various types of litigation to derail from the actual objectives of litigation in the interest of the claimants and beneficiaries?

The rapporteur sums the tools for achieving these objectives up as follows in the Explanatory Statement of his report:

"Its provisions shall safeguard the integrity of our justice system by effectively protecting European citizens from financial exploitation by litigation funders. Ensuring that victims that suffer harm receive adequate compensation is key for the Rapporteur. With this report, he wants to create a rulebook for a proactive regulation of TPLF, which will help to avoid the problems faced in third countries and which are now starting to occur also in the EU. The Rapporteur regards the following points as necessities for the upcoming legislation towards litigation funders:

- An authorization system managed by national supervisory authorities
- Strong safeguards against conflicts of interest
- Fiduciary relationship towards claimants
- Capital adequacy requirements as well as an obligation to pay adverse costs

Slide 5

- Prohibition to take control over the proceedings or withdraw without clear justification

- A cap for fees to guarantee fair and proportionate returns for claimants
- Disclosure of TPLF agreement towards the court, the claimants and the defendant

Some efforts have already been made to regulate TPLF. Recognizing the problems that stem from TPLF, Australia has recently introduced a requirement for litigation funders to hold an Australian financial services license. It has also completed a parliamentarian inquiry into the regulation of TPLF in collective redress proceedings, in which some litigation funders [at least Omni Bridgeway MD and CEO Andrew SAKER] have indicated that they would support further regulation in order to improve transparency and confidence in the system.[1] Pending legislation also exists in Canada, in the province of Ontario, where a bill reforming the collective redress regime contains provisions on TPLF."

327 amendments offered to the VOSS Report

The numerous amendments (numbers of the amendments follow below in brackets after the topic) brought by various MEPs in the JURI Committee point into various directions:

- Some strive to expand the subject matters open for funding of litigation to such topics as Environmental Matters (2), Human Rights (66), workers rights (31), and any other "public interest litigation" (15, 95, 104, 164, 173, 185) incl. Article 9 of the Aarhus Convention (56), in short all kinds of proposal of leveraging court decisions rather for exercising political pressure on decision makers and ensuring public participation in decision-making (2) for future decisions and not so much for providing compensation for injustice of the past.
- In a similarly political vein, some (e.g. 59, 107, 160, 181) want to completely prohibit third party funding of investment arbitration procedures which supposedly "Multiply the regulatory chilling effect and financial burdens for States of such proceedings and that its prohibition would protect the ability of States to legislate in the general interest" – an approach I definitively do not share considering my personal experience of various EU Member States withdrawing at will subsidies they had promised for investments into Renewable Energy Investments and for which numerous arbitration awards could only be secured with the support of third party litigation funding and after the event insurance. Commission and European Court of Justice are taking, if I may make this clear statement here, the wrong exit to a situation where they wish to keep the EU system of legal protection closed and consistent: they should offer, instead, to arbitration tribunals the possibility to submit relevant questions of EU law to the ECJ – as is apparently the solution in the south American association of states comparable to the EU. And with their current approach to investment protection arbitration, the EU really endangers the success of investments into innovations for climate change policies which are so urgently needed like power to gas and hydrogen technology.
- Other proposed amendments to the VOSS report encourage the provision of adequate public funding mentioning specifically legal aid and crowdfunding (51).

[1] Australian Parliamentary Joint Committee on Corporations and Financial Services, Litigation funding and the regulation of the class action industry, 22 December 2020, par. 16.18 on p 293.

- Some are concerned that the regulation should not create excessive administrative burdens for Member States (62).
- Some stress the need to ensure that the identity of the funder (69, 285) and at least relevant parts of the funding agreements (134) are known or – on the contrary not known at all (286, 292, 293, 294 – option to redact removed!) – to the other party, just as well as they should be known to the court, and to ensure confidentiality towards the funder who should not have access to the data in the file without the written consent of the parties.
- Some request that contractual arrangements on the basis of conditional funding should be considered as void (73).
- Some support the approach to create supervision by public authorities (81) as for similar financial services (94) and are concerned about differences between Member States due to diverging and not harmonized regulation (91).
- Some advocate that the award should always be granted to the claimants first, before the funder receives money (145), and that the funding cannot be withdrawn throughout the whole litigation (151).
- Some even wish to limit the final compensation for funders even stricter than we propose – they would grant to the funder not more than 10% of the damages awarded (186). The next strict proposal chimes in with our and the Australian proposal to ensure that the beneficiaries are not diluted to less than 70% of the compensation or damages awarded (279).
- One (314) even asks that the funders' profit be added to 100% compensation and should be paid fully by the defendant.
- Some request funders to make a financial deposit equivalent to the amount in dispute or the value in litigation with a public fiduciary (198), or to create a specific insurance fund to cover all the outstanding costs of claimants in case a litigation funder becomes insolvent. The fund shall be publicly managed and financed through annual fees payable by authorized litigation funders (202).
- None mentions legal protection insurance, sadly, which is a shortcoming considering the extensive contribution your companies provide at least in some countries to protecting consumers' interests.

We have discussed the report with several decision makers at EU level and have learned a bit about the prevailing sentiment which seems to be largely in favour of doing something (**slide 6**). Member States, though, seem very reluctant to provide serious support for funding of collective actions, and Business is very much concerned of a wave of collective actions coming up. The Commission is not in favour as it considers the initiative too much as criticism of their rules on funding in the Representative Actions Directive which, however, is not the case as funding could not be regulated comprehensively in the Representative Actions Directive for the simple reason that funding is and can be applied in much wider ways than just those regulated in the Representative Actions Directive (**slide 7**). There are too many other situations where funding is applied, particularly in the assignment model cases which already have existed before the Representative Actions Directive as can be seen from **slide 8**: there are the phenomena of legal tech platforms already growing independently of the Representative Actions Directive, and expansive legal service sites like the Netherlands and Portugal who try to attract collective actions business **(Slide 9).**

Expected modifications to the VOSS Report

The main issues which are bound to be open for consensus seem to be at least

- Common minimum statutory standards with safeguards for litigation funding such as
- Authorisation and thus a minimum supervision of funders
- Transparency and disclosure requirements
- No undue control by funders over the legal proceedings they fund and no permission to abandon funded parties except in exceptional and strictly regulated circumstances
- Claimants must receive a minimum of 60% of the gross settlement or damages
- Discretion for judges to decide *ex post* on the adequacy of legal fees and their distribution

We expect the JURI committee to vote sometime in May and could imagine a plenary vote even before the summer break. A Commission proposal, however, will – due to other urgencies like Ukraine etc. – not come forward in this Commission period but rather in the next one where it might surface around 2024 or 2025.

Evaluation of the VOSS Report, amendments and missed opportunities

Now, what do we think of the result? We think it falls short of our expectations (**Slide 10**):

1. We do not know whether there will be clear conditions to be fulfilled by funders to obtain an authorization, which scrutiny there will be on the origin of the funds to be used, which extent of supervision will be proposed.
2. It does not seem clear whether there will be constant monitoring of the market activity as is the custom for other financial market service providers.
3. Regarding funding contracts, our concern is that these are often quite complicated to read and understand, so we would like to see in each Member State and possibly at EU level a center of competence within the judiciary, i.e. the court or judicial organization, which courts can approach for assistance in evaluating the funding contracts, just as the "Fonds d'aide aux actions collectives" in Québec is able to do.
4. We think that transparency of the funding agreements should go as far also towards the defendants as letting them know all the details except for those which might be strategically abused by the defendants in an unfair way to avoid a court decision – speaking in practical terms: the court should have discretion to redact those parts which might be abused by defendants.
5. Funders should have NO influence on litigation conduct or settlement, not only NO UNDUE influence.
6. The profit potential for funders should be regulated more strictly, i.e. not more than 25% of the total proceeds should serve to compensate lawyers and funders, and that only in the most difficult and challenging situations – an idea we have taken from the Australian proposal to regulate (who would still grant 30% maximum, but not 40% as the EU legislators seems to be willing to grant).
7. A very important point is to ensure that a case like VW cannot be repeated: There, a private settlement took the case out of the court's hands which had the effect that

no court control of legaltity and fairness of the private settlement was possible any more – this must be excluded.

8. Funders should be jointly and severally liable for the adverse costs in case the claimant loses the case – the idea proposed of having a guarantee fund in the amendments sounds interesting, on top.
9. As proposed by Prof. Bruns for the transposition of the Representative Actions Directive, a public infrastructure to pay out an award obtained should be a good structural measure to ensure that there are no excessive costs for private settlement structures which funders would offer anew for each and every new case.

Slide 11 shows a comparison made of the various funding options by the funder Nivalion, who is charmingly represented at public fora – as today here – by CEO Thomas KOHLMEIER: they concede that private funding

- is very expensive, actually almost the most expensive solution (orange, left hand medium height in slide 11), with the exception of After-the-Event insurance which is even more difficult to obtain (grey, bottom left, in slide 11);
- that it only serves cases financially large enough to be of commercial interest to funders, and
- requiring book-building.

We see our preferred solution as a better one than those hitherto available in the EU and have inserted it into that chart.

But funders seem to be interested in a good cooperation with Legal Protection Insurers in order to obtain some synergies and make their services available to a broader base of consuers. Maybe this forum here can teach me some interesting news on how this might work out for the benefit of both consumers and law-abiding companies?

Let me briefly close with a comparison of the private litigation funding offers with the solution we would favor: **Slide 12** shows the usual situation of the assignment models where 25 % to 35 % or more go to funders, showing here schematically only a very moderate cost of lawyers.

Slide 13 shows the solution of the Canadian province of Québec that we would prefer in the interest of both consumers and law-abiding companies. There, only a small slice of each and every collective action goes into the central fund administered by the Québec Ministry of Justice and enables the FAAC, the “Fonds d’aide aux actions collectives”, i.e. the Fund for the assistance to collective actions, to get future collective actions going which are considered by the FAAC’s administrators to be in the publicly recognized collective interest of the beneficiaries to obtain damages – and not political influence.

Thank you very much for you attention, and I am now looking forward to a lively discussion.