Client Alert | Commercial Litigation

Not a binding rule: Court of Appeal confirms funders' costs liability not automatically capped

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Summary

On 25 February 2020, the Court of Appeal in *Chapelgate Credit Opportunity Master Fund Ltd-v-Money & Others*[1] confirmed that the liability of a commercial funder of an unsuccessful action should not automatically be limited to the amount of funding it had provided.

The Court of Appeal confirmed that the so-called Arkin cap[2] could not automatically be relied on by funders to limit their exposure to adverse costs, and endorsed the approach of Courts using their discretion in order to achieve a just result in cases involving third party funders. While acknowledging that the Arkin cap is not necessarily "*redundant*"[3], Lord Justice Newey found that "*I do not consider that the Arkin approach represents a binding rule*".[4] "*Judges…*", Newey LJ noted, "*retain a discretion and, depending on the facts, may consider it appropriate to take into account matters other than the extent of the funder's funding and not to limit the funder's liability to the amount of that funding*."[5]

Facts

The *Chapelgate* appeal arose out of a first instance decision in *Davey v Money and others*[6] (discussed in our previous alert *Link*), whereby Chapelgate had been made subject to a non-party costs order following its funding of an failed claim brought by the Claimant, Mrs Davey, against the Defendants.

In brief, in 2014, Ms Davey (the Claimant) had made serious allegations of breach of duty and dishonest conduct against the Defendants. In April 2018, the Defendants successfully defended the claims made against them, and Mr Justice Snowden ordered the Claimant to pay the Defendants' costs on an indemnity basis. The Claimant had not taken out any ATE (After-the-Event) insurance cover and failed to make the payment.

Accordingly, the Defendants requested that the Court exercise its discretion under section 51 of the Senior Costs Act 1981, and sought a non-party costs order against her commercial funder, Chapelgate. While Chapelgate accepted the non-party costs order (on an indemnity basis) should be made against it, Chapelgate argued that its total liability to the Defendants should be limited by the Arkin cap. This would have left the Defendants facing a large shortfall when it came to costs recovery.

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1 [202] EWCA Civ 246.

2 Derived from Arkin v Borchard Lines Ltd (Nos 2 and 3) [2005] EWCA Civ 655.

3 Paragraph 37.

4 Paragraph 38.

5 Paragraph 38.

6 [2019] EWHC 997.

At first instance, Snowden J refused to apply the Arkin cap principle as a matter of course and instead exercised the Court's discretion under section 51 of the Senior Costs Act 1981 to rule that Chapelgate was liable for all of the Defendants' indemnity costs incurred post the funding agreement, and not just for an amount equal to the funding it had provided during that period. Accordingly, Chapelgate, whose costs liability would otherwise have been capped at the £1.3 million that it provided in funding, was liable for an uncapped amount that was likely to be substantially more. Chapelgate appealed the decision of Snowden J to the Court of Appeal.

The Court of Appeal's decision

Dismissing the appeal, Newey LJ agreed with the approach of Snowden J in Davey, holding that the Judge's "exercise of his discretion cannot be impugned"[7] and commenting that "this was a case in which it was legitimate for a judge to attach importance to the funder's prospective gains as well as to its outlay".[8] Accordingly, Newey LJ held that it was key that the Courts exercise their discretion reasonably and take into account all the relevant circumstances of a case (and not merely the extent of a funder's funding) when deciding on liability for costs.

The Court of Appeal held that the fact alone that a funder had met only a discrete part of the total costs was not enough for the Arkin cap to protect it. Instead, the Court may consider that the funder's potential return on their investment is significant enough to warrant liability for the successful party's costs or "*the judge was entitled, too, to have regard to the extent to which the Arkin cap would leave the respondents out of pocket.*"[9]

For Newey LJ, the maturation of third party funding over the years was also important. When *Arkin* was decided, "*third party funding of litigation was still 'nascent' and conditional fee agreements and ATE insurance relatively new*"[10] and that accordingly it had been important not to deter commercial funders with the threat of disproportionate costs consequences if the litigation they funded failed. By contrast, "*a funder should now be able to protect its position by ensuring that either it or the claimant has ATE cover*" and so the risk of curtailing access to justice by deterring commercial funders on the basis that they may be ordered to meet the other side's costs is diminished. Chapelgate had considered requiring the Claimant to take out ATE insurance, which was its normal policy, but declined to do so.

For the Court of Appeal, the "more a funder had stood to gain, the closer he might be thought to be the 'real party' ordinarily ordered to pay the successful party's costs".[11] Put simply, a funder who provided the "lion's share of a claimant's costs in return for a lion's share of the potential fruits of litigation" may be ordered to "bear at the least the lion's share of the winner' costs" regardless of the actual sum of the funder's investment.[12]

Nevertheless, Newey LJ confirmed that there will still be cases where the application of the Arkin cap may be considered just. That was more likely to be the case on facts that are closely comparable to those in *Arkin*, namely in the case of "*a funder who funded only a distinct part of a claimant's costs*"[13], such as instructing an expert witness. Such specific funding of a discrete element of the litigation is, however, unlikely to be common place and so the application of the Arkin cap is likely to become rare.

7 Paragraph 44.

8 Paragraph 44.

9 Paragraph 44.

10 Paragraph 36.

11 Paragraph 38.

12 Paragraph 38.

13 Paragraph 37 and 38.

Comment

Funders can expect increasing claims for costs without the protection of the Arkin cap. Although that protection will not be abandoned altogether, following *Chapelgate*, there will likely be a more detailed consideration of the extent to which funders are likely to benefit from the claims they fund, and a greater willingness by the Courts to exercise their discretion when making costs orders against funders and to make orders that exceed the amount of funding provided. As a result, it is also highly likely that funders will invariably require claimants to take out ATE cover as part of the funding package.

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