Kluwer Mediation Blog

A New Seat at the Mediation Table? The Impact of Third-Party Funding on the Mediation Process (Part 2)

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This is the second in a series of two posts about third party funding (TPF) of litigation

Geoff's Part 1 looked at the principle of TPF. Now mediators Bill Marsh and Geoff Sharp get together to share thoughts on the impact TPF has on the mediation process

Whatever else mediation is, it is certainly a forum in which the parties have the chance to make decisions about how to resolve their dispute or conflict. Often difficult decisions. And so the factors that motivate those decisions are crucial to their choices.

In simple terms, this is often a question of carrot and stick, pros and cons.

In our experience, parties in mediation are constantly weighing the upsides and downsides of a given settlement proposal. Part of their consideration is the financial cost of losing – not just any damages, but the costs consequences as well. In many jurisdictions (including ours – England and New Zealand) the loser at trial pays (the bulk of) the winner's legal costs, and so that cost forms an important part of considering 'what happens if we actually lose our case?'

Traditionally, a litigating party bears both the upside and the downside risk. If they win, they receive. If they lose, they pay. But TPF radically changes this. And therefore changes the whole consideration of risk. For example, a funded claimant can win the case (and sure, they have to share the winnings with a funder); but if they lose, someone else will pay the costs. In fact, the funder *has paid* the costs and there is *no recourse*. So, they feel that they have an upside without a downside – a 'free run' at the case.

And for most people, that changes *everything;*

More Confident Claimants

Funded claimants appear more confident in settlement negotiations, because as we say, they consider they face an upside but no downside. They have managed to secure a safety net. The main question in their mind is the size of that upside!

Another Brain

A fresh perspective is one of the more important impacts on the mediation process – funders will naturally scrutinise a case before agreeing to fund it undertaking quite sophisticated due diligence, and some may want a say in settlement decisions. That means that an additional legal mind has assessed the case, at least at the outset, and no doubt at key stages along the way as well.

In practice, funders will sometimes be present at the mediation. Given the nature of their involvement, they can add a wise head and tend to act as a useful check and balance on the funded party.

The Mere Threat of Funding

Allied to there being another brain in the mix, the mere fact that a claimant has been able to secure funding – can sometimes, in and of itself, lead to mediation and /or settlement.

> As James Rogers, a Norton Rose Fulbright arbitration partner says;
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> I was involved in a somewhat unusual +5 year case where the threat of funding led dramatically to settlement… We eventually had four arbitration awards in hand that we were getting ready to enforce and we were preparing another round of claims… The threat of funding confirmed our client's persistence and, within a month confirming that we had engaged funders, the Chinese party agreed to settle. It was a very powerful tool.

And that is perhaps why some claimants are sometimes happy to volunteer the existence (and sometimes details) of their funding to the other side, as it can send a very strong message about the merits of the claim and the wisdom of settling now rather than later as the escalating scale of payments to the funder ramps up the closer to trial it gets.

As a mediator, Geoff was recently asked to examine a party's funding agreement and, while they were not prepared to show it to the other side, he was asked to confirm that a funding agreement was in place together with some of the more salient details that, strategically, the claimant wanted the defendant to know about.

A More Dispassionate View

Funders will often approach settlement discussions much more dispassionately than

the parties themselves.

Their concern – understandably – is less with the underlying issues that generated the dispute in the first place (after all, they weren't even there) and more with the risk analysis that underpins settlement discussions.

> Steven Friel, CEO at Woodsford Litigation Funding says;
>
> As a funder, our main concern is in achieving a financial return. If a claimant wants something else, for example vindication on some point of principle, then this introduces the prospect that the claimant's interest will not always be aligned with our interest. We approach such cases with caution.

Put simply, funders are normally focused on the numbers. This can of course be very valuable. But it can occasionally run the risk of steering the mediation discussions away from a perhaps more personal exchange of views when the parties themselves may need these to get to a money settlement.

Neither focus need be to the exclusion of the other, but the balance is worth thinking about if you are a mediator.

Funders in the Mediation Room

Mediators report that they are seeing funders at the mediation table, and that this sets up an interesting dynamic. Having a repeat user brain with a dispassionate view on mediation day can be invaluable – especially if the funders and the funded interests are aligned as they should be.

So, if funders do attend mediation, what role do they typically play at the table… silent observer, active participant, agent of reality?

> Ruth Stackpool-Moore, Director of Litigation Funding at Harbour Litigation Funding says;
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> Although rare, if and when we attend mediations, our role is generally one of silent observer. The indirect effect of our presence may be the same as our involvement in the case generally, in that the other side feels the weight of our experience and may be more constrained in trying to "pull the wool" over the claimants eyes. What we wish to avoid is that our presence diverts the other side's attention from settlement, which would be counter-productive for all involved.

Whose Case is it Anyway?

Exactly who calls the shots, whether to take the case to mediation in the first place or

a decision around what level of settlement is appropriate, can be a contentious issue.

There is a concern in some quarters that funders will gradually progress from funding, to controlling, to hands on – which would not be a lot different from a law firm on a contingency fee and lawyers do worry about the degree of control a funder might have.

Indeed, in a 2016 litigation finance survey of over 400 litigators by US litigation funder, Lake Whillans , it was the economic terms of any arrangement that were of most importance to respondents when choosing a funder and a close second came a funder's right to influence or decide strategy or settlement.

But the funders we spoke to don't seek drop-dead control – quite the opposite in fact, as Ruth Stackpool-Moore at Harbour explains;

> The decision on the appropriateness or otherwise of mediation is one for the claimant and their legal team. At Harbour, we do not control how the claimant and their legal team deal with the dispute. In our experience, mediation employed at strategically sensible stages of a dispute can be a very effective way to reach settlement or narrow the issues which remain in dispute, thereby often reducing the uncertainties and cost of the proceedings.

Consistent with that, Steven Friel at Woodsford;

> Ultimately, we don't decide. The decision whether or not to mediate a case, much like any other important step in the cases we fund, rests with the litigant and their lawyers. Of course, we have input into the decision, and it may be the case that we have the option whether or not to extend our funding to cover the mediation.
>
> When providing our input, and when deciding whether to extend funding to cover mediation, the factors we take into account are exactly the same factors that any reasonable litigant should take into account. In other words, is the mediation reasonably likely to lead to settlement, or otherwise narrow the issues in dispute?
>
> At Woodsford, we are staffed largely by English lawyers, trained in a post-Woolf approach to alternative dispute resolution, so we are relatively open to mediation.

It would seem to us when there is a prospect of *settling* the dispute, there is perhaps more chance of a tussle over control. Selvyn Seidel of US funder Fulbrook Management acknowledges that a funder "may not have a lot to say over a settlement – we don't want to make the decision but we have to be able to voice our opinion".

Again, funders appear to have a fairly consistent approach, with Steven Friel reporting that;

> Ultimate control rests with the claimant and the claimant's lawyers. We have the right to provide input, but we don't necessarily have veto rights. Ultimately, however, my objective as a commercial funder is to ensure that I choose and cultivate the relationships with my claimants in such a way that I rely on cooperation, rather than strict contractual rights, when advancing my position in relation to settlement

Consistent with all of this is the voluntary code of the Association of Third Party Funders (England and Wales) that requires a funder "not seek to influence the Funded Party's solicitor or barrister to cede control or conduct of the dispute to the Funder" and requires the Litigation Funding Agreement to state whether (and if so how) the funder may provide input into decisions around settlement. The guiding principle being that a lawyer should exercise independent professional judgement and give candid advice regardless of the involvement of a funder.

If there is a dispute the Code requires it to be referred to a Queen's Counsel instructed jointly or nominated by the Bar Council for a binding opinion.

In a very useful e-book by Steven Friel and Jonathan Barnes Litigation Funding 2017 we are taken on a world tour of third-party funding jurisdictions. Of interest, in the context of this post, are questions around funder's ability to participate in the settlement process (e.g. mediation) and to veto settlement.

While there appear small regional differences, in most jurisdictions it is perfectly acceptable that funders participate in settlement proceedings, including attending mediation and the good reasons why they should do so are acknowledged.

If there is a veto power in respect of settlement, that would normally be found in the funding agreement and in some jurisdictions it seems it is common practice to include it (for instance, Switzerland and Germany).

In New Zealand the existence of a funder's veto was tested in the courts and a fairly liberal approach was taken in *Strathboss Kiwifruit v Attorney-General* where the defendant (the Crown) was concerned at the funder's power of veto in relation to settlement.

> The NZ High Court was not persuaded;
>
> In this case, it was argued that too much control vested with the funder… The Crown was also concerned at the funder's effective power of veto in relation to settlement of the proceedings…
>
> I am not persuaded that the terms of the deed with the funder in this case are necessarily inappropriate for a representative action of this type.

> There is likely to be a range of views as to what would constitute an acceptable settlement, or the circumstances in which the plaintiffs may be better advised to explore alternatives for bringing the claims to an end. As between the claimants, the committee representing them will have to strive for consensus, and on major issues will no doubt be cognisant of the attitude of the funder. In most scenarios, I accept Mr Dunning's point that the claimants and the funder should continue to have aligned interests…
>
> The funder will therefore need to maintain their goodwill to carry on with the action. That goodwill would be in jeopardy if the funder wanted to continue when the claimants considered an acceptable settlement was available…
>
> More importantly, the mechanisms for resolving major disputes contemplate the involvement of independent third parties with appropriate expertise. Reputationally, if in no other respect, that will provide a fetter on the funder's ability to act unreasonably.

But control can be exercised in the number of ways and the ability to walk away can give a funder de facto control over the way a case is conducted – while it is hard to generalise, in one of the very few examples of a Litigation Funding Agreement we could find online (Roland Prozess Finanz AG), any agreement reached by mediation required Roland's consent. In the event of the funded and funder failing to agree on a settlement proposal, the agreement could be terminated – with the party refusing settlement paying to the other the amount they would have been entitled to under the agreement if settlement had been reached – in the example agreement this meant a funded/funder split of 70/30 for any sum under €500,000 and an 80/20 split for sums exceeding that (and at mediation, a split of 80/20 applied).

But there is no doubt, the more uncertainty around who is the decision maker in the mediation room, the harder it is as a mediator to read the room.

Funders Stand in 'Their' Party's Shoes

Following the English Court of Appeal's recent decision in Excalibur Ventures v Texas Keystone, it is clear that funders (at least in England and Wales) cannot just fund the case and then stand back.

Conduct of the funded party will, at least in its consequences, be attributed to them even though, as we see above, funders may not want or have the ability to influence strategy.

In Excalibur the funder provided both litigation funding and security for the Defendant's costs. The funded claimant, Excalibur Ventures, lost heavily at trial with the judge describing the claim as "speculative and opportunistic". The Claimant (and hence the funder) was ordered to pay the Defendant's costs on an indemnity basis, because of the Claimant's – not the funder's – conduct.

In response to their objections, Tomlinson LJ said: 'The argument for the funders

boiled down to the proposition that it is not appropriate to direct them to pay costs on the indemnity basis if they have themselves been guilty of no discreditable conduct or conduct which can be criticised.

"Even on the assumption that the funders were guilty of no conduct which can properly be criticised, and I accept that they did nothing discreditable in the sense of being morally reprehensible or even improper, this argument suffers from two fatal defects…"

"First, it overlooks that the conduct of the parties is but one factor to be taken into account in the overall evaluation. Second, it looks at the question from only one point of view, that of the funder…. It ignores the character of the action which the funder has funded and its effect on the defendants… A litigant may find himself liable to pay indemnity costs on account of the conduct of those whom he has chosen to engage – e.g. lawyers, or experts who may themselves have been chosen by the lawyers, or witnesses… The position of the funder is directly analogous".

'By funding, the funder takes a risk, a risk as to the nature of which he has the opportunity to inform himself both before offering funding and during the course of the litigation which he funds,' he added.

Two Surprising Benefits

Early Settlement

Funding may change the timing dynamics – counterintuitively, it may make early settlement more attractive given that funding agreements often provide for a sliding payment scale – depending if the matter concludes early, middle or late in the journey towards trial. There will often be a lower percentage payable to a funder on any settlement in a mediation room compared to a win in the court or arbitration room – simply because the interplay between costs and risk changes the closer to adjudication the case gets.

> Ruth Stackpool-Moore at Harbour again;
>
> The certainty of a guaranteed return from settlement following a successful mediation is generally worth more to us than the uncertainty of what may, or may not, come through a judgment or award…

Better Informed Parties

Perhaps a surprising spin-off benefit from third-party funding is that there will inevitably be an increase in the number of better informed litigants, regardless of whether those parties actually receive funding – as Victoria Shannon Sahani from Washington and Lee University School of Law says over at the Kluwer Arbitration Blog; since funders fund only a small percentage of the cases they are asked to look at (may be less than 1% to around 5%) there are far more cases that are *not* funded then cases that *are* funded.

That means funders are providing “free” case assessments to the vast majority of parties they encounter, regardless of whether they decide to finance the case or not. Parties who are rejected and who receive a substantive explanation will be better informed to make a call on their future direction of travel.

As Victoria Shannon Sahani says “over time, an increase in the number of well-informed parties will have a very positive impact on our international system of dispute resolution”

Last Word

Mediations are often a heady cocktail of upsides, downsides and risk analysis.

In one sense, TPF changes nothing. But in another very real sense, it seats another stakeholder at the actual or metaphorical mediation table – and as all mediators know, that changes everything.

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