

PART III

ACCESS TO JUSTICE AND COSTS OF LITIGATION

CHAPTER 7

PRIVATE FUNDING

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<https://www.cplj.org/publications/3-7-private-funding>

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1 INTRODUCTION

1.1 Private Funding and Access to Justice: Fundamental Policy Questions

- 1 The question of who must bear the costs of a lawsuit is fundamental for the law of civil procedure (on cost allocation in general, see chapter 5) and has therefore always had considerable significance for legislators, courts and academics. In contrast, the initially much more pressing problem for the parties of where to get the financial resources they need for litigation only came to public attention much later. Even then, this issue was mostly seen as a matter of providing affordable access to justice, which led to the question to what extent the state should exempt indigent parties from paying court fees and, if necessary, also pay their lawyers' fees (see chapter 6). However, the more the willingness or power of states to provide such 'public funding' diminishes, the more the question of 'private funding' comes to the fore.¹ Indeed, a shift from public to private funding has been observed in many jurisdictions in recent decades, although the reasons for this may vary: be it the dwindling financial power of the state, be it the belief in the superiority of market-based models over welfarist models.
- 2 Of particular interest in this chapter is not so much business models but rather how legal frameworks for the various forms of private funding are structured in the legal systems under study and how this regulation, or non-regulation respectively, affects access to justice. This leads to a number of questions that cannot be answered here in a general way, but should at least be briefly outlined in advance. First of all, recourse to non-state players as guarantors of access to state courts raises issues of accountability and transparency.² Another obvious and fundamental policy question is whether private funding requires special regulation because it tends to lead to more litigation (and thus to more workload of the courts) and could encourage aggressive and uncompromising litigation strategies, or whether, on the contrary, it should be promoted because it proves indispensable in ensuring access to justice for indigent parties (ie, consumers, but also middle-class individuals and small and medium-sized enterprises). As far as can be seen, such aspects have mainly been discussed with regard to the admission of commercial third-party litigation funding (see below para 47), but the issue of 'justice for profit'³ or 'commodification of justice'⁴ is basically relevant for all private funding instruments. Another

¹ On the emergence of private forms of litigation funding in the wake of gradual decline in civil legal aid, see, for example, M Ahmed and X Kramer, 'Global Developments and Challenges in Costs and Funding of Civil Justice' (2021) *Erasmus Law Review* 181, 184–185.

² WH van Boom, 'Financing Civil Litigation by the European Insurance Industry' in M Tuil and L Visscher (ed), *New Trends in Financing Civil Litigation in Euro: A Legal, Empirical, and Economic Analysis* (Elgar 2010) 92, 94.

³ See J Kalajdzic / P Cashman / A Longmoore, 'Justice for Profit: A Comparative Analysis of Australian, Canadian and U.S. Third Party Litigation Funding' (2013) 61(1) *American Journal of Comparative Law* 93.

⁴ On the cultural background of the 'anti-commodification argument', see A Cordina 'Is It All That Fishy? A Critical Review of the Concerns Surrounding Third Party Litigation Funding in Europe' (2021) *Erasmus Law Review* 270, 274–275.

question is whether the concern sometimes expressed that private funding is unfair because it is typically only available to plaintiffs but not to defendants (or plaintiffs seeking relief other than a money judgment) seems justified and, if so, applies equally to all instruments.

- 3 At this point, it should also be mentioned that the availability or lack of funds might not only influence the litigation behaviour of the funded party, but also that of the opponent and even the court: Does a party that cannot avail itself of state or private support tend to be treated more accommodatingly or leniently or, conversely, is there even a risk that such a party will be made rather more difficult to maintain its position in the proceedings because, from the point of view of the court and the opponent, it seems less likely that the judgment will be challenged with an even more costly appeal?

1.2 Private Funding, Legal Aid and General Rules on Costs

- 4 Since legal aid is a form of social assistance, it is typically understood to be subsidiary by nature and is generally only available where self-help is not possible. Thus, private funding plays an important role either when a legal system does not provide any legal aid for private law cases or when parties are too wealthy to be eligible, but not wealthy enough to conduct proceedings with their own means. This suggests that it is mainly the ‘forgotten middle’⁵ – middle-class individuals and small and medium-sized enterprises – that rely on private funding.⁶ Apparently, however, parties that are not budget-constrained are also resorting to the services of litigation funders in order to save their own resources.⁷
- 5 Beyond the question of the availability of legal aid, there are further connections between the importance of private funding and the actual and legal framework of litigation costs. Overall, the higher and unpredictable the court and legal fees (see chapter 4), the more important funding becomes: If a legal system fails to reduce litigation costs or at least make them sufficiently transparent and proportionate, there is a growing need to allow forms of private litigation financing.⁸ Furthermore, the rules on cost allocation are relevant (see chapter 5): In systems where the loser bears all or at least nearly all costs, the higher the risk of losing, the more important (but also the more expensive) funding becomes. On the other hand, if an indigent party, even if it wins, must bear its own costs

⁵ For this term in the context of legal cost financing, see International Bar Association, *Legal Expenses Insurance and Access to Justice* (2019) 9 <<https://www.ibanet.org/MediaHandler?id=98236046-737B-4F05-A964-B7F438F04CD8>> accessed 15 February 2023. See also M Trebilcock / A Duggan / L Sossin (ed), *Middle Income Access to Justice* (University of Toronto Press 2012).

⁶ Cf M Reimann (ed), *Cost and Fee Allocation in Civil Procedure – A Comparative Study* (Springer 2012) 39.

⁷ For various reasons why litigants, either poor or rich, take advantage of third funding, see P Beasley and B Summerfield, ‘The users of litigation finance – who, where, when and why?’ in S Friel (ed), *The Law and Business of Litigation Finance* (Bloomsbury 2020) 319, para 10.55 ff.

⁸ On the relationship between these two regulatory tasks, see M Ahmed and X Kramer (2021) *Erasmus Law Review* 181, 185–186.

or at least a significant part of them (the so-called recoverability gap), it will in any case depend on funding.

1.3 Scope of this Chapter

- 6 As this chapter is about the financing of civil proceedings, the possibility for parties to obtain legal advice from private providers, either free of charge or for a fee, in extrajudicial matters is not discussed.⁹ The same applies to the professional duty of lawyers to inform their clients about the availability of financing options.¹⁰ Contractual clauses with which one party attempts to oblige the other to bear the costs in the event of a court dispute have a certain proximity to our topic; such models are nevertheless not dealt with here because they are not about financing but about avoiding litigation costs.¹¹
- 7 In line with the thematic scope of the CPLJ project, the chapter will mainly focus on individual lawsuits, primarily in domestic cases. The particular problems of private funding in the field of consumer disputes, collective redress and arbitration¹² should be addressed at least briefly. The financing of insolvency proceedings, criminal defence and public law disputes is excluded.

2 CATEGORIES OF PRIVATE FUNDING

- 8 Some fundamental categories of private funding shall be established from the outset, since they determine the structure of the further presentation in this chapter: (2.1) provision against the financial risks of litigation before or after the inception of the dispute, (2.2) passive as opposed to active funding, and (2.3) commercial as opposed to altruistic funding.

2.1 Precautionary Measures for Future Disputes versus Financing Existing Disputes

- 9 There are different ways in which the discussion of the various instruments grouped in this chapter could be structured. One conceivable way would be to distinguish according to who provides the funds (such as a commercial litigation funder, an insurance

⁹ On legal advice from lawyers employed by insurance companies, see WH van Boom in M Tuil and L Visscher (n 2) 92, 97–98. On the advice landscape and the relevance of ‘legal helplines’ in the UK, see Civil Justice Council, *The Law and Practicalities of Before-The-Event (BTE) Insurance* (2017) 74 ff <<https://www.judiciary.uk/wp-content/uploads/2017/11/cjc-bte-report.pdf>> accessed 15 February 2023; C Hodges, *Delivering Dispute Resolution – A holistic Review of Models in England and Wales* (CH Beck Hard Nomos 2019) 201 ff.

¹⁰ On this topic, see Civil Justice Council (n 9); *Blackstone’s Civil Practice 2022* (Oxford UP 2022) para 5.3 ff; C Toms, ‘Insurance’ in S Friel (n 7) 227, para 8.75.

¹¹ For a comparative overview, see A Cabral, ‘Procedural Contracts about the Costs of Civil Litigation: a Brazilian view in Comparative Perspective’, (2022) *Yearbook of Socio-Economic Constitutions* 245.

¹² On the issue of funding other forms of ADR, which will not be discussed here, see M Ahmed and X Kramer (2021) *Erasmus Law Review* 181, 186–188.

company, a law firm, a non-profit organisation, the employer or family of the party). A more instructive option, favoured here, is to first distinguish whether private funding is a precautionary measure to hedge against financial risks of future litigation (below paras 13-15) or a matter of financing a dispute that has already arisen or is even already pending in court (below paras 42-75). In terms of insurance law, this dichotomy corresponds to the distinction between before-the-event insurance (BTE) and after-the-event insurance (ATE) (see below paras 16-41).

- 10 This distinction is not only important from a systematic legal perspective, but also from an economic one: A party who makes provisions for a future and uncertain legal dispute only has to incur relatively low costs (in the form of membership fees or insurance premiums), but has to accept that these costs may prove to be unnecessary ex post because the case for which provisions were made may never occur. In contrast, the need for financing is established when the dispute or even litigation has already occurred, although financing then becomes considerably more expensive because a third party will typically only agree to bear the costs if it receives a significant fee or a share of the party's hoped-for profit in return.¹³ This also has the consequence that the financing of an already existing dispute is more suitable for a plaintiff than for a defendant: unlike the plaintiff's claim, the position of the defendant, even if he or she wins the case, normally has no evident asset value in which the financier can participate.¹⁴ But even from the fact that a defendant tends to find it more difficult to find a financier, it does not necessarily follow that the state would be entitled or even obliged, for reasons of equal treatment, to prohibit the plaintiff from having recourse to litigation funding as well.¹⁵

2.2 Passive versus Active Funding

- 11 All of the constellations mentioned so far have in common that someone provides the financial means for a legal dispute, but does not take over the conduct of the case in court or even become a party to the proceedings. However, there are alternatives to such passive funding. This becomes apparent when the law firm entrusted with the conduct of the case also bears the preliminary financing, ie, initially assumes the costs for the court and the taking of evidence, and also only receives a fee if the case is ultimately won. A second, somewhat more far-reaching model of active funding is that the alleged creditor even transfers the claim to the financier, who can then assert it as assignee in its own name in court. One could say that with passive funding the money comes to the

¹³ Cf GM Solas, *Third Party Funding: Law, Economics and Policy* (Cambridge UP 2019) 163.

¹⁴ Cf WH van Boom, 'Litigation costs and third-party funding' in WH van Boom (ed), *Litigation, Costs, Funding and Behaviour – Implications for the Law* (Routledge 2017) 5, 9; C Toms (n 10) para 8.78.

¹⁵ See A Stadler, 'Third Party Funding of Mass Litigation in Germany: Entrepreneurial Parties – Curse or Blessing?' in L Cadiet / B Hess / M Requejo Isidro (ed) *Privatizing Dispute Resolution: Trends and Limits* (Nomos 2019) 209, 224.

litigation, while with active funding the litigation comes to the money.¹⁶ At least in principle, both models can help create the financial conditions for law enforcement and both raise similar policy issues. However, in many jurisdictions, additional problems arise with active forms of financing, particularly with regard to the admissibility of contingency fees or assignments for the purpose of litigation or debt collection (see below paras 64-68).

2.3 Commercial versus Altruistic Funding

- 12 Normally, third parties only provide funds for another party's legal dispute if they gain a financial benefit in return (a fee, insurance premiums, or a share in the profits of the client). It is precisely this economic self-interest of the funder and the associated phenomenon of a certain 'commercialization of law enforcement' that raises questions to be discussed in this chapter (see above para 2). If commercial funders must try hard to pick the sure winners among the likely winners, it seems at least doubtful that third-party funding enhances access to justice for those parties whose chances of success are rather slim anyway.¹⁷ However, there are also various constellations of practical relevance in which charitable individuals or associations provide support motivated by the public interest at stake, which can be high even if the prospect of a profitable or at least favourable judgement is rather low (see below chapter 6).

3 PRECAUTIONARY MEASURES FOR FUTURE DISPUTES

3.1 Membership in Solidarity Groups

- 13 Much older than the 20th century business model of legal expenses insurance (see below paras 16 et seq), or rather some kind of historical predecessor, are solidarity groups that, among other benefits, offer their members support in financing legal proceedings that may become necessary. Traditional examples of this are the guilds of craftsmen and merchants.¹⁸ So-called legal service plans offered, eg, by trade unions or associations of farmers, tenants or landowners still have the same function today. One should note,

¹⁶ On the distinction between passive and active funding models, see GM Solas (n 13) 138 ff. M Reimann (n 6) 47–48, proposes a terminologically different but in substance similar distinction, namely between 'assignment of claims' and 'outside litigation funding'.

¹⁷ On this interesting aspect, see V Shannon Sahani, 'The Impact of Third-Party Funding on Access to Justice', (2022) Yearbook of Socio-Economic Constitutions 29.

¹⁸ For an example from the 1669 statute of a local barber surgeons' guild in Germany see P Hellwege, *From Guild Welfare to Bismarck Care: professional guilds and the origins of modern social security law and insurance law in Germany* (Duncker & Humblot 2020) 55 f: 'As it also happens that somebody infringes a master of this guild, and also children or servants, in their good name [...], so shall henceforth the costs, which have to be spent for bringing justice to the profession and its intermediaries, be given and taken from the entire [...] guild'. For comparative perspectives on the relevance of professional guilds as predecessors of modern insurance systems (but without particular reference to the coverage of legal costs) see the contributions in P Hellwege (ed), *Professional Guilds and the History of Insurance – A Comparative Analysis* (Duncker & Humblot 2020).

however, that legal service plans usually do not focus on funding of litigation, but rather on legal advice and document drafting.¹⁹

- 14 Families can play a similar role as solidarity groups. This is reflected in provisions whereby a family law maintenance claim may include funding for necessary litigation. For an example, see Sec 1360a(IV) Bürgerliches Gesetzbuch (Civil Code) (Germany): 'If a spouse is not in a position to bear the costs of a legal dispute which relates to a personal matter, the other spouse has a duty to advance him these costs, insofar as this is equitable.'²⁰

3.2 Contractual Obligation to Assume Litigation Cost Risks

- 15 The cases mentioned so far have in common that support in the event of a lawsuit is only a secondary aspect: a member of a family or guild may be able to claim coverage for legal costs paid, but most people do not marry or join a guild for this very reason. Similarly, a company pursuing any purpose may also be obliged, inter alia, to provide a shareholder, under certain conditions, with the necessary means to bring an action against a third party on behalf of the company.²¹ In such a broad sense, one can also classify the conclusion of other contracts, which as such have nothing to do with litigation, as provision for potential litigation cost risks. This applies to employment contracts, in particular with regard to lawsuits related to the professional activity of employees and their potential liability towards third parties. In some countries, it seems to be common for employers to promise to pay the employee's legal fees in the event of a dispute with a third party;²² in other countries (such as Germany) it is assumed, even without an explicit contractual provision, that the employer may be obliged to indemnify the employee against litigation costs in such cases.

3.3 Legal Expenses Insurance

3.3.1 Introduction

- 16 The model of legal expenses insurance (also known as legal cost insurance, legal protection insurance or simply legal insurance²³) can be seen as a specialised combination of

¹⁹ For the similarities and differences between US-style legal service plans and legal protection insurance, see T Raiser, 'Legal insurance', in NJ Smelser and P Baltes (ed), *International encyclopedia of the social & behavioral sciences* (vol 13, 1st edn, Elsevier 2001) para 4; M Faure and J De Mot, 'Comparing Third-Party Financing of Litigation and Legal Expenses Insurance' (2012) 8 *Journal of Law, Economics & Policy* 743, 747–748, 751–752; M Kilian and F Regan, 'Legal Expenses Insurance and Legal Aid – Two Sides of the Same Coin? The Experience from Germany and Sweden' (2004) 11(3) *International Journal of the Legal Profession* 233, 236–237. On BTE cover for members of affinity groups and unions in the UK see Civil Justice Council (n 9) 110 ff.

²⁰ On the similar situation in Switzerland see I Jent-Sørensen in P Oberhammer / T Domej / U Haas, *Schweizerische Zivilprozessordnung* (Helbing Lichtenhahn, 3rd ed 2021) Art 117 para 19.

²¹ See W Chen, *A Comparative Study of Funding Shareholder Litigation* (Springer 2017) 189 ff.

²² On employer-provided BTE insurance in the UK see Civil Justice Council (n 9) 118.

²³ T Raiser (n 19) para 1.

the two approaches mentioned above to protect against future litigation cost risks: The potential litigant concludes a contract by which the contracting party (the insurer) undertakes to bear possible litigation costs, and at the same time joins a solidarity group (namely the group of policyholders) and thus spreads the risk over many heads. There seems to be rather little comparative law research on legal expenses insurance, especially when one considers how much attention is paid to other private financing models, namely contingency fees and, more recently, third-party funding.²⁴

- 17 A generally useful description of legal expenses insurance can be found in Art 198(1) of the EU Solvency II Directive:²⁵ ‘an insurance undertaking promises, against the payment of a premium, to bear the costs of legal proceedings and to provide other services directly linked to insurance cover, in particular with a view to the following: (a) securing compensation for the loss, damage or injury suffered by the insured person, by settlement out of court or through civil or criminal proceedings; (b) defending or representing the insured person in civil, criminal, administrative or other proceedings or in respect of any claim made against that person.’
- 18 The insurance cover usually includes the fees of the policyholder's lawyer; in addition, the court costs including costs of taking evidence and, if applicable, the costs of the prevailing opponent, which are to be borne by the policyholder.²⁶ Normally, the insurance company provides its service either by reimbursing the costs incurred by its client or by indemnifying the client against the claims of its creditors (ie, the other party and, as regards court costs, the state).

3.3.2 Availability and Regulation of Legal Expenses Insurance

- 19 Originally, the business model of legal expenses insurance was a mere by-product in ordinary policies: under contracts insuring, eg, automobiles, buildings or private or professional liability risks,²⁷ the assumption of legal costs was promised as one of several

²⁴ For a recent comparative overview in Korean language, see Judicial Policy Research Institute (South Korea), *Research on the Legal Services Insurance* (2021) <<https://jpri.scourt.go.kr/post/post-View.do?boardSeq=32&menuSeq=35&lang=en&seq=1265>> accessed 15 May 2023.

²⁵ Directive on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), Directive 2009/138/EC of 25 November 2009. A translation of the more complex definition in Art L127-1 Code des Assurances (Insurance Code) (France) reads: ‘A legal expenses insurance transaction is any transaction consisting, in return for the payment of a premium or contribution agreed in advance, in paying the costs of proceedings or providing services arising from the insurance cover, in the event of a dispute or litigation between the insured and a third party, with a view in particular to defending or representing the insured in civil, criminal, administrative or other proceedings or against a claim against him or her or to obtaining amicable compensation for the damage suffered.’ For a much shorter, yet wider description (not restricted to court proceedings) see Sec 125 Gesetz über den Versicherungsvertrag (Insurance Contract Act) (Germany): ‘In the case of legal expenses insurance, the insurer shall be liable to the extent necessary to look after the legal interests of the policyholder or of the insured person as per the agreement.’

²⁶ M Reimann (n 6) 39; C Toms (n 10) para 8.64.

²⁷ On specific problems of D&O (director and officers) insurance cf C Toms (n 10) para 8.68–8.71.

benefits.²⁸ While such ‘package-deal insurance’ is still available, widespread and thus relatively inexpensive, legal expenses insurance also gradually developed as a stand-alone product specifically designed to protect against the financial risks of litigation. This product is relatively common in some countries, notably in continental Europe and Japan.²⁹ In 2020, the 44 legal expenses insurance companies operating in Germany collected almost EUR 4,400 million in premiums and provided benefits to insured persons amounting to almost EUR 3,259 million.³⁰ In 2017, 95 per cent of households in Sweden had legal expenses insurance which is automatically included as part of household insurance policies.³¹ In contrast, legal expenses insurance plays a much smaller role in other jurisdictions, especially in the common law world³² or Russia. With regard to stand-alone insurance cover, this also applies to the UK,³³ although such policies have been available there for decades and were strongly recommended in the Jackson Report to small and medium-sized enterprises and households.³⁴

- 20 The prevalence of legal expenses insurance in the various jurisdictions is obviously related to the amount and to the predictability of the costs associated with litigation.³⁵ Only if the expected costs are high does it seem sensible to take out insurance, which is then all the more expensive and therefore unaffordable for many. If litigation costs are difficult to calculate in individual cases, insurance companies will provide for lump sums or coverage caps, which in turn makes such policies less attractive for the target group. On the other hand, it seems speculative to consider whether the demand for legal expenses insurance in different countries is related to the different degree of litigiousness of the citizens.³⁶

²⁸ Cf C Hodges (n 9) 135: ‘a tick-box add on to household or motor insurance’; M Reimann (n 6) 39–40: ‘package-deal insurance’.

²⁹ See C Hodges / S Vogenauer / M Tulibacka, *The Costs and Funding of Civil Litigation – A Comparative Perspective* (CH Beck Hart 2010) 21; International Bar Association (n 5) 14 ff. However, see also M Faure and J De Mot (n 19) 743, 744: ‘not as widespread in Europe as it is often alleged’.

³⁰ Gesamtverband der Deutschen Versicherungswirtschaft (German Insurance Association), *Statistical Yearbook of German Insurance 2021* (2021) table 82 <<https://www.gdv.de/en/statistical-yearbook-2021-72318>> accessed 18 January 2022.

³¹ International Bar Association (n 5) 21.

³² See International Bar Association (n 5) 14 ff.

³³ Cf Civil Justice Council (n 9) 97 ff; International Bar Association (n 5) 22–23; J Sorabji, ‘Legal Expenses Insurance and the Future of Effective Litigation Funding’ (2021) *Erasmus Law Review* 189; C Toms (n 10) para 8.67.

³⁴ R Jackson, *Review of Civil Litigation Costs: Final Report* (2010) 71 ff <<https://www.judiciary.uk/wp-content/uploads/JCO/Documents/Reports/jackson-final-report-140110.pdf>> accessed 15 February 2023.

³⁵ Cf T Raiser (n 19) para 2; C Hodges / S Vogenauer / M Tulibacka (n 29) 106; International Bar Association (n 5) 30–33. For a detailed analysis of the relationship between the availability of legal expenses insurance and the search for predictable litigation costs, see J Sorabji (2021) *Erasmus Law Review* 189, 194–196.

³⁶ Cf WH van Boom in M Tuil and L Visscher (n 2) 92, 94–95.

- 21 Legal expenses insurance is subject to general national rules for the protection of policyholders and supervision of insurance undertakings.³⁷ There is only a rudimentary unification of these rules at international level, namely within the European Union (and the European Economic Area³⁸). There, the relevant rules were originally introduced by the 1987 EEC Directive on Legal Expenses Insurance³⁹ and are now contained in Art 198–205 of the already-mentioned 2009 EU Solvency II Directive.⁴⁰ It seems remarkable that the International Association of Legal Protection Insurance (Rencontres Internationales des Assureurs Défense – RIAD), representing insurers from Europe, Canada, South Africa and Japan, in its Code of Conduct requires all its members, also those operating outside the EU, to recognise the rules of the Directive as minimum standards.⁴¹

3.3.3 Scope of Application and Preconditions of Cover

- 22 As a rule, in BTE legal expenses insurance it is not relevant whether the policyholder will be involved in the proceedings as plaintiff or defendant. However, legal expenses coverage purchased as a mere by-product of liability insurance policies is typically only significant for potential defendants, whereas stand-alone policies also cover the filing of lawsuits and are in practice more important for potential plaintiffs – but are more expensive for that reason alone.⁴²
- 23 If coverage of legal costs is a mere by-product of an ordinary insurance policy, the scope of cover is related to the main subject matter of the insurance (eg, for motor vehicles, buildings or personal liability risks). But even stand-alone legal expenses insurance only covers the agreed types, not all types of disputes. Typically, legal expenses insurers offer various product modules that are specifically tailored either to certain groups of policyholders (ie, private households, employees, self-employed, farmers, companies, associations, etc) or to certain areas of life (ie, contractual disputes, road traffic, real estate, etc) and that customers can combine to suit their specific needs.⁴³ In Germany, a common bundle includes legal protection as regards ‘private, job, traffic’ (‘Privat, Beruf,

³⁷ For a comparative account of the regulation of legal cost insurance in 18 countries, see M Kilian, ‘Determinanten des europäischen Rechtsschutzversicherungsmarkts – Beratungsmonopole, Anwaltsgebühren und Kostenerstattung’ (1999) 88 Zeitschrift für die gesamte Versicherungswissenschaft 23.

³⁸ See Decision of the EEA Joint Committee amending Annex IX (Financial services) to the EEA Agreement, 78/2011 of 1 July 2011.

³⁹ Directive on the coordination of laws, regulations and administrative provisions relating to legal expenses insurance, Directive 87/344/EEC of 22 June 1987.

⁴⁰ Directive on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), Directive 2009/138/EC of 25 November 2009.

⁴¹ International Association of Legal Protection Insurance, *Code of Conduct as amended on 23 April 2015*, Introduction <<https://legalprotectioninternational.com/code-of-conduct>> accessed 15 February 2023.

⁴² WH van Boom in M Tuil and L Visscher (n 2) 92, 93; M Reimann (n 6) 39–40; AK Mayrhofer and B Gsell, ‘The Financial Obstacles of the Access to the Judge’ in M Schmidt-Kessel (ed), *German National Reports on the 21st International Congress of Comparative Law* (Mohr Siebeck 2022) 223, 247.

⁴³ For an instructive comparative table of scope of coverage in consumer BTE policies, see Civil Justice Council (n 9) 25 ff. See also International Bar Association (n 5) 23 ff.

Verkehr').⁴⁴ As a rule, legal protection is excluded for family and inheritance law matters as well as for all sorts of disputes within the policyholder's family.⁴⁵ Exclusions for disputes about investments and loan agreements are also of practical importance. The insurance conditions specify whether legal protection should only apply to domestic court proceedings or also in cross-border cases.

- 24 It is in the nature of an insurance contract that only the risk of a future uncertain event is covered. In consequence, there is no coverage if the dispute is already looming or if litigation has even already begun (for the specificity of UK style after-the-event legal expenses insurance, see below paras 45-46). In this respect, difficult questions can arise with regard to the interpretation and transparency of the clauses defining the temporal scope of the insurance cover. Therefore, the contracts often provide that the policyholder only enjoys insurance cover after the expiry of a waiting period.
- 25 Even when a dispute falls within the material and temporal scope of the policy, the insurance company normally reserves the right to pay the policyholder's costs only if the litigation has a reasonable prospect of success.⁴⁶ It is questionable whether the insurer's assessment of the merits may not only take into account the position of its policyholder, but also the arguments of the potential opponent.⁴⁷ Moreover, the audit often goes so far as to exclude even the costs of promising litigation if the legal action can be considered mischievous or wanton. While it is sometimes pointed out that the audit by insurers typically is not quite as comprehensive and intensive as that of a commercial litigation funder,⁴⁸ this cannot be generalised, and when it comes to an amount in dispute that is so high that it would also be of interest to TPFs, there should hardly be any difference.
- 26 If the insurer agrees in principle to cover the claim, the policyholder is still obliged to keep the costs as low as possible and to choose the most cost-effective between different possible courses of action. Irrespective of whether this duty to minimise costs is only derived abstractly from the law or is described in more detail in the insurance conditions,

⁴⁴ In 2022, such an insurance package cost between EUR 208 and EUR 683 per year, depending on the insurer, with a deductible of EUR 150 in the event of a claim. Cf <www.test.de/Rechtsschutzversicherung-im-Vergleich-4776988-0> accessed 15 February 2023.

⁴⁵ An extension to family law matters is often recommended; see, eg, Council of Bars and Law Societies of Europe, *CCBE Position on Legal Expenses Insurance* (31 January 2017) para II.4 <https://www.ccbe.eu/fileadmin/speciality_distribution/public/documents/INSURANCE/INS_Position_papers/EN_INS_20170331_CCBE-Position-on-legal-expenses-insurance.pdf> accessed 15 February 2023.

⁴⁶ For details, see Civil Justice Council (n 9) 64 ff.

⁴⁷ In Germany, a clause that allows the insurer to carry out such an extensive examination was held to be invalid: Case IV ZR 221/19 [Federal Court of Justice of Germany], Judgment 31 March 2021 [ECLI:DE:BGH:2021:310321UIVZR.221.19.0].

⁴⁸ Cf AK Mayrhofer and B Gsell in M Schmidt-Kessel (n 42) 223, 247.

the policyholder can often hardly assess for which litigation measures he may claim cover.⁴⁹

3.3.4 Disputes between Insurer and Policyholder

- 27 The best insurance is worth little if it does not pay out in the very case in which it is really needed. As with any insurance policy, there can be a variety of disagreements between the insurer and the policyholder about whether or not the conditions for claiming on the insurance are met. In the case of legal expenses insurance, however, this is particularly problematic, because the policyholder can be caught between two fronts: He or she is not primarily concerned with the claim against the insurance company, but with the legal dispute with another party, which he or she wants to finance with the help of the insurance company. If the insurer refuses to cover, it delays the policyholder's legal action against the other party. There is even the threat of a definitive loss if the main legal action becomes futile due to the statute of limitations before the insurance company provides the necessary funds for it. To make matters worse, legal expenses insurance usually expressly excludes coverage for claims by the policyholder against the insurer.
- 28 An additional problem exists from the policyholder's point of view if the company offering the legal expenses insurance also sells other types of insurance. This may lead to conflicts of interest if the legal expenses insurer either covers the policyholder both in respect of legal expenses and in respect of another class of insurance or is at the same time the liability insurer of the policyholder's opponent. In order to prevent legal expenses coverage from being denied for self-interested reasons, some European countries had prohibited insurance undertakings from pursuing within the same territory legal expenses insurance and other classes of insurance. However, such prohibitions were

⁴⁹ In 2019, the Federal Court of Justice of Germany (Case IV ZR 279/17 [Federal Court of Justice of Germany], Judgment 14 August 2019 [ECLI:DE:BGH:2019:140819UIVZR279.17.0]) declared a clause invalid that had been typical until then to be non-transparent. This clause stipulated the following:

'[T]he legal costs should be kept as low as possible. Of several possible courses of action, the policyholder must choose the most cost-effective one. For example (list not exhaustive), he must:

- not conduct two or more lawsuits if the objective can be achieved more cost-effectively with one lawsuit (eg, bundling claims or claiming joint and several debtors as joint litigants, extending a lawsuit instead of filing a separate lawsuit),
- waive (additional) claims that are not or not yet necessary in the current situation,
- await the final decision in other court proceedings which may have factual or legal significance for the intended legal dispute before filing an action,
- only bring an action for an appropriate part of the claims in advance and postpone any necessary judicial assertion of the remaining claims until the decision on the partial claims has become final, [...].

The policyholder shall obtain and follow the instructions of the insurer in order to mitigate the loss. He shall instruct the lawyer in accordance with the instruction.

If one of the obligations mentioned [...] is intentionally breached, the policyholder shall lose his insurance cover. In the event of a grossly negligent breach of an obligation, the insurer is entitled to reduce his benefit in proportion to the severity of the policyholder's fault.'

already abolished by Art 8 of the 1987 EEC Directive on Legal Expenses Insurance.⁵⁰ The same follows today from Art 205 of the 2009 EU Solvency II Directive.⁵¹ The Directive rather attempts to mitigate the problem by requiring that different insurance contracts of the same policyholder be separate (Art 199). In addition, conflicts of interest in the management of claims must be avoided, either by separating work areas within the insurance company or by entrusting the management of claims in respect of legal expenses insurance to an undertaking having separate legal personality (Art 200). Pointing in the same direction, the RIAD Code of Conduct⁵² requires that insurers shall arrange their business activities so as to prevent situations where conflicts of interest could arise (§ 3) and make use of specialised and qualified staff, whose sole duty is the management of claims and the provision of legal advice, excluding any similar responsibilities in other classes of insurance (§ 4).

- 29 With regard to the settlement of disputes between a legal expenses insurer and the insured party concerning coverage or an alleged conflict of interest, Art 203 and 204 of the EU Solvency II Directive require Member States to provide for arbitration or any other procedure offering comparable guarantees of objectivity, without prejudice to the right of appeal to a judicial body available under national law.⁵³ Member States have some leeway in implementing this provision. For example, in Germany, Sec 128 Gesetz über den Versicherungsvertrag (Insurance Contract Act) applies, which reads as follows: ‘In the event that the insurer denies his liability because looking after the legal interests does not have sufficient prospects of success or is wanton, the contract of insurance must provide for a procedure to call in expert opinion or another procedure with comparable guarantees of impartiality in which a decision can be taken regarding the differences of opinion between the parties concerning the prospects of success or the wantonness of prosecution. The insurer shall draw the policyholder's attention to this fact when denying his obligation to effect payment. If the contract of insurance does not provide for any such procedure or the insurer fails to provide this information, the policyholder's need for legal protection shall be deemed to have been acknowledged in individual cases.’ For jurisdictions in which the applicable law does not prescribe arbitration, § 2 of the RIAD Code of Conduct⁵⁴ provides that insurers shall choose a solution for the settlement of the dispute with the policyholder which best meets the demands of

⁵⁰ Directive on the coordination of laws, regulations and administrative provisions relating to legal expenses insurance, Directive 87/344/EEC of 22 June 1987.

⁵¹ Directive on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), Directive 2009/138/EC of 25 November 2009.

⁵² International Association of Legal Protection Insurance, Code of Conduct (n 41).

⁵³ Directive on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), Directive 2009/138/EC of 25 November 2009. See also Recital 83 of the Directive: ‘Conflicts between insured persons and insurance undertakings covering legal expenses should be settled in the fairest and speediest manner possible. It is therefore appropriate that Member States provide for an arbitration procedure or a procedure offering comparable guarantees.’

⁵⁴ International Association of Legal Protection Insurance, Code of Conduct (n 41).

fairness, promptness, feasibility and efficiency. In doing so, insurers must ensure that the procedure established does not deter the policyholder from taking advantage of it.

- 30 A very detailed and remarkably policyholder-friendly regulation is provided in France. A translation of Art L127-4 Codes des Assurances reads: '(1) The contract shall stipulate that in the event of disagreement between the insurer and the insured concerning the measures to be taken to settle a dispute, this disagreement may be submitted to the assessment of a third party designated by mutual agreement by the parties or, failing this, by the president of the court ruling on the merits of the case in accordance with the accelerated procedure. The costs incurred for the implementation of this option shall be borne by the insurer. However, the president of the court ruling on the merits of the case may decide otherwise where the insured has exercised this option in abusive conditions. (2) If the insured has initiated litigation at his own expense and obtains a more favourable solution than that proposed by the insurer or by the third party mentioned in the previous paragraph, the insurer shall compensate him for the costs incurred in the exercise of this action, within the limit of the amount of the guarantee. (3) When the procedure referred to in the first paragraph of this article is used, the time limit for legal action is suspended for all legal proceedings covered by the insurance guarantee and which the insured may initiate as a claim, until the third party responsible for proposing a solution has made its position known.'
- 31 If one considers state support to be only subsidiary to private provision, the question arises whether a party can claim legal aid even though he or she has taken out legal expenses insurance. It follows from this principle of subsidiarity that legal aid is excluded if the insurance company has already promised coverage. If, on the other hand, the insurer refuses coverage, it is questionable whether the policyholder is required to first challenge the insurer's decision. This is the situation in Germany and Switzerland, for example. However, if the attempt to settle the dispute with the insurer out of court fails, the policyholder is at least not obliged to file a lawsuit against the insurer before he or she can obtain legal aid.⁵⁵

3.3.5 *Insurer's Influence on the Conduct of the Case*

- 32 While the policyholder has an interest in taking all necessary legal measures to resolve the insured dispute in his or her favour, the insurance company is primarily concerned with keeping costs as low as possible. In a legal system where the losing party has to bear the costs of the litigation, the insurance company tends to have a greater interest in its client winning than in a system where each party has to bear its own costs. Ultimately, however, insurers will try in any case to reserve some influence on the conduct

⁵⁵ Germany: see P S Weinmann, 'Die Gewährung von Prozesskostenhilfe im Zivilprozess vor der ordentlichen Gerichtsbarkeit trotz bestehender Rechtsschutzversicherung' (2020) *Recht und Schaden* 78. Switzerland: see I Jent-Sørensen (n 20) Art 117 para 21.

of the case.⁵⁶ This can be done, for example, by offering the services of mediators or by stipulating that the costs of court proceedings are only covered if the attempt to settle the dispute out of court has failed. Often, there is an obligation on the part of the policyholder to first coordinate all steps that incur costs (eg, hiring a lawyer, filing a lawsuit or lodging an appeal) with the insurer. It should be noted, however, that in some jurisdictions the court may exceptionally order a non-party to pay the costs of the proceedings and that the risk of such a third-party cost order may also exist for a legal expenses insurer if it interferes improperly in the conduct of the policyholder's litigation.⁵⁷

- 33 A limit for the insurer's influence that today is widely recognised in principle but often unclear in detail is the policyholder's fundamental right to free choice of lawyer. This is to prevent a principal-agent conflict that arises when a lawyer who regularly works with an insurance company, or is even its employee, has the company's cost interests in mind rather than the success of the client. Art 200(4) and Art 201 of the EU Solvency II Directive⁵⁸ enshrine both the right of free choice of lawyer and the insurer's duty to draw the policyholder's attention to it; Member States may provide for exceptions only under narrow conditions for cases arising from the use of road vehicles (Art 202). It follows, for example, that a legal expenses insurer which stipulates that legal assistance will in principle be provided by its employees is precluded from also providing that the costs of legal assistance by a lawyer chosen freely by the insured person will be covered only if the insurer takes the view that the handling of the case must be subcontracted to an external lawyer; this applies irrespectively of whether or not legal assistance is compulsory under national law in the proceedings concerned.⁵⁹ Even in cases where a large number of insured persons suffered loss as a result of the same event, the legal expenses insurer may not reserve the right to select the legal representative of all insured persons concerned.⁶⁰
- 34 The insurance contract may neither release the insurer from its contractual obligations if policyholders mandate a lawyer to represent their interests without the consent of the company, nor restrict the pool of eligible lawyers to those residing in the district of the court.⁶¹ However, it is often argued that the Directive allows a certain degree of

⁵⁶ This is critically assessed, for example, by Council of Bars and Law Societies of Europe, *CCBE Position on Legal Expenses Insurance* (n 45) para II.3.

⁵⁷ On the requirements for such an order based on 'unjustified intermeddling' under English law, see *Travelers Insurance Company Ltd v XYZ* (Supreme Court, UK), Judgment 30 October 2019 [2019 UKSC 48].

⁵⁸ Directive on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II), Directive 2009/138/EC of 25 November 2009.

⁵⁹ *Jan Sneller v DAS Nederlandse Rechtsbijstand Verzekeringsmaatschappij NV*, Case C-442/12 (CJEU), Judgment 7 November 2013 [ECLI:EU:C:2013:717].

⁶⁰ *Erhard Eschig v UNIQA Sachversicherung AG*, Case C-199/08 (CJEU), Judgment 10 September 2009 [ECLI:EU:C:2009:538].

⁶¹ *Pascal Nobile v DAS Rechtsschutz-Versicherungs AG*, Case E-21/16 (EFTA Court) Judgment 27 October 2017.

nudging:⁶² For example, the insurer is free to offer its clients to participate in the selection of the lawyer⁶³ and to grant them benefits (such as reduced premiums) if they agree to do so or to be advised by a lawyer selected by the insurer.⁶⁴ The Council of Bars and Law Societies of Europe, however, considers such influence permissible only within very narrow limits.⁶⁵ The insurer may also reserve the right to appoint a lawyer for a policyholder who refrains from legal representation, if this appears necessary to them.

3.3.6 Access to Legal Expenses Insurance and Obstruction of Justice?

- 35 One conceivable and sometimes actually raised objection to legal expenses insurance is that, rather than facilitating access to justice, it may tempt policyholders to burden the courts with unnecessary cases.⁶⁶ From this point of view, legal expenses insurance does not enable access to justice, but an obstruction of justice. However, it seems questionable whether there is really cause for this concern.⁶⁷ It is already doubtful whether, under otherwise comparable circumstances, more cases are brought in jurisdictions where legal expenses insurance is widespread than in others. Even if this were true, the objection would still depend on whether parties who can fall back on legal expenses insurance lose more often in court than others; for only from this could one conclude whether insured parties are more inclined to file unfounded or possibly even abusive lawsuits or defences. Although generalising conclusions are difficult, it seems more likely that the insurance companies, when they examine their clients' cases (see above para 25), rather have a certain filter effect, thus ultimately even tend to relieve the courts.⁶⁸ It is equally difficult to make reliable statements about the relationship between legal expenses insurance and parties' willingness to settle, because this depends not only on the specific

⁶² On the different scope of the right in various EU and non-EU jurisdictions, see the overview by International Bar Association (n 5) 27 ff.

⁶³ See, however, Art L127-3(4) Code des Assurances (Insurance Code) (France), which prohibits the insurer from proposing the name of a lawyer to the insured without a written request.

⁶⁴ For a discussion on the admissibility of such 'efficiency agreements' in Germany see P Gottwald, 'Funding Civil Litigation Through Legal Expenses Insurance in Germany' in R Assy and A Higgins, *Principles, Procedure, and Justice: Essays in honour of Adrian Zuckerman* (Oxford UP 2020) 199, 202–203. On the controversial question of the scope of the right to choose the lawyer in the UK, see Civil Justice Council (n 9) 152 ff.

⁶⁵ Council of Bars and Law Societies of Europe, *CCBE Position on Legal Expenses Insurance* (n 45) paras I.1 and II.1.

⁶⁶ Such accusations, especially from lawyers and judges in Germany, are reported by T Raiser (n 19) para 5; M Kilian, 'Alternatives to Public Provision: The Role of Legal Expenses Insurance in Broadening Access to Justice – The German Experience' (2003) 30 *Journal of Law and Society* 31, 45.

⁶⁷ A very balanced analysis is provided by J De Mot / M Faure / L Visscher, 'TPF and its alternatives – An economic appraisal' in WH van Boom (n 14) 31, 42–44.

⁶⁸ Empirical studies in Germany point in this direction; see P Gottwald (n 64) 201; PL Murray and R Stürner, *German Civil Justice* (Carolina Academic Press 2004) 124; M Kilian (2003) 30 *Journal of Law and Society* 31, 46. See also L Visscher and T Schepens, 'A Law and Economics Approach to Cost Shifting, Fee Arrangements and Legal Expense Insurance' in M Tuil and L Visscher (n 2) 7, 23.

insurance conditions but also on the procedural framework in general.⁶⁹ On altruistic funding of litigation by non-commercial supporters, see below paras 76 et seq.

3.3.7 Access to Legal Expenses Insurance and Access to Justice

- 36 In the context of Part 4 of the Compendium on Comparative Civil Justice, it is of particular interest to what extent legal expenses insurance can be understood as an instrument for opening up or at least enhancing access to justice. This is precisely the promise with which insurers advertise such policies: the International Association of Legal Protection Insurance (RIAD) advocates the high potential of legal expenses insurance as an easy, affordable and high-quality solution for access to justice and the law. This is already expressed in the introduction to the Association's Code of Conduct: 'Legal Protection Insurance provides access to justice, legal advice and representation for policyholders by providing assistance and financial resources in order to enable policyholders to exercise and enforce their legal rights.'⁷⁰
- 37 There is probably hardly a jurisdiction today in which the legal aid system for civil cases is so generously designed that there is no access to justice problem and citizens can simply free ride on the state, ie, save the costs of legal expenses insurance or similar precautionary measures because they can always count on state support if necessary. However, the aforementioned position of the insurance industry seems overly optimistic, even in those jurisdictions where legal expenses insurance is widespread. It should be recalled that the existence of legal expenses insurance could temporarily preclude access to legal aid even if the insurer initially refuses to provide cover (see above para 27). Furthermore, it seems particularly doubtful whether legal expenses insurance improves the chances of enforcing small claims: Since policies usually provide for a deductible, the costs of low value disputes are not covered. However, even if there is cover, this does not lead to an increase in the lawyer's fee, and so the policyholder is left with the problem of finding a lawyer who is prepared to take on the case.⁷¹
- 38 There is a whole range of additional practical problems. For example, it has occasionally been reported that parties often do not even think about the fact that they have legal expenses insurance; this can happen in particular if this insurance is only a package-deal component of another insurance contract.⁷² In contrast, stand-alone legal expenses insurance policies are relatively expensive and therefore tend to be purchased by those who could also finance a rather unlikely legal dispute from their own funds in an emergency.⁷³ It fits in with this that the success of legal expenses insurance is at least not

⁶⁹ Cf C Hodges / S Vogenauer / M Tulibacka (n 29) 95.

⁷⁰ International Association of Legal Protection Insurance, Code of Conduct (n 41).

⁷¹ Cf M Kilian (2003) 30 Journal of Law and Society 31, 46.

⁷² See Civil Justice Council (n 9) 134–135; International Bar Association (n 5) 20.

⁷³ Empirical studies in Germany show a correlation between high income and willingness to take out legal costs insurance; cf M Kilian (2003) 30 Journal of Law and Society 31, 46–48.

necessarily related to insufficient or receding state support;⁷⁴ rather, in some jurisdictions the number of such insurance policies increased in the second half of the 20th century in parallel with the expansion of the legal aid system at that time.⁷⁵ A notable example in recent years are the mass lawsuits in connection with the ‘Diesel scandal’ in Germany: by the end of 2021, German legal protection insurers had paid out a total of more than EUR 1,200 million to their policyholders in 380,000 cases for lawyers’ fees, court costs and expert witness fees, with the average amount in dispute per case being around EUR 26,000.⁷⁶ Even assuming that many of these cases would never have reached court without legal expenses insurance, it is remarkable that it is mainly the owners of relatively expensive vehicles who benefit from insurance. For such parties, most of whom are probably neither entitled to nor dependent on legal aid, legal expenses insurance seems to be a ‘nice-to-have’ rather than a ‘must-have’.

- 39 On the other hand, anyone who conducts civil proceedings not only very rarely, but more frequently as plaintiff or defendant, ie business people and commercial enterprises, faces the problem of finding an insurer at all.⁷⁷ Even if such a client succeeds in doing so, it should be borne in mind that the insurer normally reserves the right to cancel the contract for the future after an insured event. Against this background, the prospect of consumer associations acquiring legal protection policies to cover themselves for future class actions seems completely futile.⁷⁸
- 40 It can be assumed that legal expenses insurance could be offered at more affordable prices if the number of policyholders increases significantly. From the perspective of national legislation, however, this can only be brought about with considerable effort, since the supply of and demand for such insurance is related to two parameters that are difficult to influence, namely the amount and the predictability of costs associated with litigation (see above para 20). Most citizens can also hardly estimate how likely it is for them to be involved in a legal dispute; obviously, many people tend to be too optimistic

⁷⁴ A correlation between the increase in legal expenses insurance and the decrease in legal aid has been demonstrated, eg, for the Netherlands: BCJ van Velthoven and CM Klein Haarhuis, ‘Legal Aid and Legal Expenses Insurance, Complements or Substitutes? The Case of the Netherlands’ (2011) 8(3) *Journal of Empirical Legal Studies* 587.

⁷⁵ See M Kilian and F Regan (n 19) 233: ‘While in some societies the decline of legal aid created a vacuum of mechanisms to ameliorate the effects of market failure, Legal Expense Insurance (LEI) developed as an additional solution. That is, LEI also developed in a number of societies at approximately the same time that publicly funded legal aid emerged and flourished.’

⁷⁶ Gesamtverband der Deutschen Versicherungswirtschaft (German Insurance Association), Press release of 19 November 2021 <<https://www.gdv.de/de/medien/aktuell/prozesskosten-im-diesel-skandal-steigen-auf-1-2-milliarden-euro--72406>> accessed 18 January 2022.

⁷⁷ On the situation in Germany, where in practice even small or medium-sized enterprises cannot take out legal expenses insurance, see P Gottwald (n 64) 203 and 207. For further reasons why legal expenses insurance is only limited available for particular litigious individuals see M Faure and J De Mot (n 19) 759–760.

⁷⁸ Cf A Stadler, ‘German collective actions – is litigation funding in a dead end?’ in X Kramer / J Hoevenaars / B Kas / E Themeli (ed), *Frontiers in Civil Justice* (Elgar 2022) 260, 264–265.

in this respect.⁷⁹ But even those who are considering taking out legal expenses insurance face the problem of comparing the various products and prices and finding the right insurance package for their needs.⁸⁰ If a state were to simply restrict access to legal aid in order to give citizens an impetus to take out private legal expenses insurance, it would run the risk of ending up with those least able to finance litigation without any public or private support.⁸¹

- 41 Against this background, it has been discussed whether it might seem sensible to make the conclusion of legal expenses insurance policies compulsory, at least for certain groups of potential parties.⁸² Behind this is the idea that the need to litigate in court is a stroke of fate that can befall anyone (similar to illness, unemployment or accident), and it therefore seems essential to ensure that every individual makes provisions for this. In this model, however, the private insurance companies would have to be willing, or possibly even legally obliged, to offer appropriate legal protection insurance; alternatively, public insurance companies would have to step in. Overall, the introduction of mandatory legal expenses insurance seems hardly advisable, and it stands to reason that it would make more sense for states to invest in their legal aid systems instead.⁸³

4 FINANCING EXISTING DISPUTES: PASSIVE FUNDING

- 42 With regard to the passive financing of litigation that has already arisen, the following observations look first at the supply side and then at the demand side.

4.1 Supply Side of Litigation Funding

- 43 The providers addressed here are banks, insurance companies and specialised litigation funding companies. In particularly complex cases, a combination and coordination of

⁷⁹ See, for example, J Sorabji (2021) *Erasmus Law Review* 189, 192.

⁸⁰ Valuable help is provided by non-profit organisations that regularly publish analyses of products and prices. For Germany, see the publications of 'Stiftung Warentest': <www.test.de/Rechtsschutzversicherung-im-Vergleich-4776988-0> accessed 15 February 2023.

⁸¹ For the Netherlands, see BCJ van Velthoven and CM Klein Haarhuis (2011) 8(3) *Journal of Empirical Legal Studies* 587, 606: 'the shift from legal aid to LEI has some clear disadvantages for low-income citizens'. A remarkable special case is Sweden, where at the end of the 20th century the previously exceptionally generous legal aid system could be scaled back without much social resistance precisely because most Swedes already had legal expenses insurance anyway. See F Regan, 'The Swedish Legal Services Policy Remix: The Shift from Public Legal Aid to Private Legal Expense Insurance' (2003) 30 *Journal of Law and Society* 49.

⁸² For an early plea for mandatory legal expenses insurance in Germany, see F Baur, 'Armenrecht und Rechtsschutzversicherung' (1972) 27 *JuristenZeitung* 75, 77–78. For the UK, see R Lewis, 'Litigation Costs and Before-the-event Insurance: The Key to Access to Justice?' (2011) 74 *Modern Law Review* 272; more recently J Sorabji (2021) *Erasmus Law Review* 189, 192–194, who pleads for a reinvigorated legal expenses insurance scheme available to all forms of civil claims and mandatory for all citizens.

⁸³ For Germany, see P Gottwald (n 64) 200; for the UK, see Civil Justice Council (n 9) 125 ff. Other authors share this basic conviction, but consider it simply unrealistic that the state will be willing to invest more in legal aid again in the foreseeable future; cf J Sorabji (2021) *Erasmus Law Review* 189: 'the age of legal aid has passed'.

various public and private funders may be appropriate,⁸⁴ as may be a change of the funding strategy during the course of litigation.⁸⁵ The financial participation of law firms will only be discussed later in connection with active funding (below paras 64-70).

4.1.1 Banks

- 44 In practice, taking out an ordinary bank loan is probably the most obvious and frequently chosen option for a party who is involved in a dispute and needs to raise the funds for litigation. From a procedural point of view, this option is not particularly noteworthy, as the lender retains full control of the case and the bank cannot claim more than repayment of the loan, regardless of whether the lawsuit is won or not. However, the situation is different in the case of a so-called non-recourse loan, where the loan only has to be repaid if the borrower is successful.⁸⁶ In either situation, it should be noted that bank loans as a financing option usually only benefit alleged creditors (ie, potential claimants), as they can offer their alleged claim to the bank as collateral. Impecunious alleged debtors, on the other hand, will find it much more difficult to convince a bank to grant a loan with the help of which they can defend against a lawsuit or even file an action for a negative declaration.

4.1.2 Insurance Companies

- 45 As already mentioned, potential parties can take out legal expenses insurance 'just in case', long before a dispute or legal proceedings are in contemplation. Such ordinary before-the-event insurance (BTE) is to be distinguished from after-the-event insurance (ATE). The latter is a variant of third-party litigation funding by insurance companies which is available in some jurisdictions, notably the UK, but also Canada, Australia⁸⁷ and Germany.⁸⁸ At first sight, one might think that ATE is at odds with general principles of insurance law: although an insurance contract may exceptionally provide retroactive protection for a period that has already passed, this only applies if the insured has no knowledge that the insured event has already occurred.⁸⁹ However, ATE can still be

⁸⁴ For an extraordinary example from the Netherlands (the Dexia case with more than 300,000 claimants), see IN Tzankova, 'Funding of mass disputes: lessons from the Netherlands' (2012) 8 *Journal of Law, Economics & Policy* 549, 551 ff.

⁸⁵ Cf Blackstone's Civil Practice 2022 (n 10) para 5.4.

⁸⁶ For the difference between traditional and non-recourse loans as a means of funding, see WH van Boom in WH van Boom (n 14) 5, 9–10.

⁸⁷ See V Waye and V Morabito, 'Financial arrangements with litigation funders and law firms in Australian class actions' in WH van Boom (n 14) 155, 159.

⁸⁸ A Stadler in L Cadiet / B Hess / M Requejo Isidro (n 15) 209, 212–213. In Germany, some insurers offer the subsequent conclusion of a legal expenses insurance contract when the alleged victim of a traffic accident intends to file a claim for damages and seeks protection against the cost risk of losing the case. However, this happens rather rarely and is considerably more expensive than a standard BTE policy.

⁸⁹ See, for example, the Principles of European Insurance Contract Law 2015, Art 2:401(2): 'If, in the case of retroactive cover, the policyholder knows at the time of the conclusion of the contract that the

classified as a true insurance: This is because the future, uncertain risk is not the dispute or litigation in which the policyholder is already involved, but the question of whether the policyholder will incur costs as a result.⁹⁰ However, because this risk is typically very high, ATE is significantly more expensive than BTE. Another difference is that most ATE policies only cover the costs of the opposing party to be borne by the policyholder (adverse costs) and maybe the own disbursements, but not the fees of the policyholder's own lawyers.⁹¹

- 46 Where ATE insurance is legally permissible, it is usually only used by claimants for larger amounts in dispute and is often taken out as a supplement to a 'no win no fee' agreement with the party's lawyer (see below para 64). From the customers' point of view, it is an advantage that the providers have to comply with the requirements of insurance supervisory law. Nevertheless, the business model is subject to a whole range of criticisms, and accordingly in the UK it was judged much more sceptically by the Jackson Report than BTE.⁹² As a result, its attractiveness was significantly reduced in 2012: since then, the policyholder, if he or she wins the case, can no longer claim reimbursement of the insurance premium paid from the loser; an exception only applies to premiums for a policy insuring against the risk of incurring a liability to pay expert reports in respect of clinical negligence.⁹³ However, a plaintiff may still expect certain benefits from taking out ATE insurance and disclosing this at trial: On the one hand, this can release him or her from the obligation to provide security for litigation costs, and on the other hand, it is reported that under these circumstances the defendant is often more willing to settle.⁹⁴ At least in this respect, it can still be said that, however limited the range of suitable scenarios may be in practice, ATE insurance can also make a certain contribution to access to justice.

4.1.3 Litigation Funding Companies

- 47 In essence, commercial litigation funding is understood to mean 'the provision by a funder to a funded party of financial support for the costs of, and where applicable the risks related to, the resolution of a legal dispute, based on a funding agreement, in exchange for a remuneration or reimbursement that is dependent upon the outcome of the

insured event has occurred, the insurer shall [...] provide cover only for the period after the time of the conclusion of the contract'. For the text of the Principles, see <<https://www.uibk.ac.at/zivilrecht/forschung/evip/restatement/sprachfassungen/peicl-en.pdf>> (accessed 26 February 2023); for the text, comments and comparative notes, see J Basedow / J Birds / M Clarke / H Cousy / H Heiss / L Loacker, *Principles of European Insurance Contract Law* (2nd edn, Otto Schmidt 2016) Art 2:401.

⁹⁰ See M Kilian and F Regan (n 19) 235.

⁹¹ C Toms (n 10) para 8.72; Blackstone's Civil Practice 2022 (n 10) para 5.14.

⁹² See R Jackson (n 34) 80 ff.

⁹³ Sec 58C Courts and Legal Services Act 1990 (UK), introduced by Sec 46 Legal Aid, Sentencing and Punishment of Offenders Act 2012 (UK). For the discussion on the abolishment of the recoverability of ATE premiums, see C Hodges (n 9) 141 ff., 281.

⁹⁴ C Toms (n 10) para 8.80–8.82.

dispute’.⁹⁵ The possibility of such financing civil proceedings through specialised companies (or entrepreneurs) in exchange for a share in the profits has certainly been one of the most discussed and perhaps most controversial issues worldwide in procedural law in recent years. Several comparative studies look not only at various legal systems,⁹⁶ but also at differences and similarities between third-party funding and other public and private litigation funding options.⁹⁷ In the following, the development in some jurisdictions and the impact of commercial third-party funding on the conduct of civil proceedings will be briefly outlined.

4.1.3.1 Comparative Overview

- 48 In contrast to taking out an ordinary bank loan to finance a lawsuit, it is considered problematic in many jurisdictions if the money comes from a funder who conducts such transactions commercially, especially if the funder demands a share of the hoped-for profit from the lawsuit. In common law jurisdictions, these concerns are reflected in the traditional criminal law and tort law prohibitions against third parties encouraging to bring a lawsuit through intermeddling (‘maintenance’) or financially supporting a plaintiff so that the plaintiff can litigate on the condition that the third party will receive a share of the proceed if successful (‘champerty’).⁹⁸ Quite similar in approach, in those civil law countries where success-based fees are still excluded or severely restricted (see below para 67), the policy problem is addressed that it is difficult to see why commercial financiers should be allowed to do what the much stricter regulated lawyers are prohibited from doing.⁹⁹ The UK Supreme Court has also clarified in a much-noticed new judgement that the agreement with a third party litigation funder is subject to the general requirements for the validity of damages-based agreements (DBAs) if the funder is (as usual)

⁹⁵ See the definition in the Code of Conduct (No 1(d)) of the European Litigation Funders Association <<https://elfassociation.eu/about/code-of-conduct>> accessed 15 February 2023.

⁹⁶ The following comparative books in English language are particularly worth mentioning from recent times: W Chen (n 21); S Friel (n 7); L Bench Nieuwveld and V Shannon Sahani (ed), *Third-Party Funding in International Arbitration* (2nd edn, Wolters Kluwer 2017); N Rowles-Davies, *Third Party Litigation Funding* (Oxford UP 2014); GM Solas (n 13); B Zhang, *Third Party Funding for Dispute Resolution: A Comparative Study of England, Hong Kong, Singapore, the Netherlands, and Mainland China* (Springer 2021). In addition, there are many essays in journals and books and even specialised print and online periodicals with regular reports from several jurisdictions (see ‘Third Party Litigation Funding Law Review’ <<https://thelawreviews.co.uk/title/the-third-party-litigation-funding-law-review>> accessed 15 May 2023; ‘Litigation Finance Journal’ <<https://litigationfinancejournal.com>> accessed 15 May 2023). Early but still influential articles can be found in (2012) 8(3) *Journal of Law, Economics & Policy*.

⁹⁷ See, for example, WH van Boom in WH van Boom (n 14) 5; B Deffains and C Desrieux, ‘To litigate or not to litigate? The impacts of third-party financing on litigation’ (2015) 43 *International Review of Law and Economics* 178; J De Mot / M Faure / L Visscher (n 67) 31; M Faure and J De Mot (n 19) 743; S Voet, ‘Costs and funding of collective redress proceedings’ in A Stadler / E Jeuland / V Smith (ed), *Mass Litigation in Europe: Model Rules for Effective Dispute Resolution* (Elgar 2020) 264.

⁹⁸ For details and the historic background of these doctrines, see N Rowles-Davies (n 96) 22 ff.

⁹⁹ On a highly traditionalist perspective, see A Bruns, ‘Third-Party Financing in the Perspective of German Law – Useful Instrument for Improvement of the Civil Justice System or Speculative Immoral Investment?’ (2012) 8 *Journal of Law, Economics & Policy* 525, 531 ff.

entitled to a percentage of the success of the litigation.¹⁰⁰ Where funding is considered to be the granting of a loan and is measured against the corresponding regulations, the accusation of usury can also be raised.¹⁰¹ In some jurisdictions, traditional prohibitions have been increasingly softened by case law or replaced by more specific provisions. The trend seems to be that third party financing is now being legalised, at least in principle, in more and more common law and civil law jurisdictions,¹⁰² although the degree and density of legal regulation vary greatly.¹⁰³

- 49 In some regions where the legal situation is considered to be still insufficiently clarified, a funding market has nevertheless developed.¹⁰⁴ In others, there is a push for explicit regulation to create a reliable legal framework. This is evident, for example, in the USA and in the European Union, where there is an intensive discussion whether it would make sense to have a uniform regulation that welcomes and allows third-party funding in principle, but defines effective rules to prevent abuse.¹⁰⁵ The European Parliament shows particular interest in the topic of ‘responsible private funding of litigation’: Following a series of preparatory studies,¹⁰⁶ the Parliament published a formal resolution

¹⁰⁰ *R (on the application of PACCAR Inc and others) v Competition Appeal Tribunal* (Supreme Court, UK), Judgment 26 July 2023 [2023 UKSC 28].

¹⁰¹ Cf, for example, L Bench Nieuwveld and V Shannon Sahani (n 96) 15.

¹⁰² However, a remarkable, highly restrictive approach is still taken however in Ireland, where the situation is exacerbated by the absence of legal aid for non-family civil cases. For a critical account, see D Capper, ‘Litigation Funding in Ireland’ (2021) *Erasmus Law Review* 211.

¹⁰³ Cf, for example, GM Solas (n 13) 120–122. On the different degrees of regulation, see V Shannon Sahani, ‘Global Laboratories of Third-Party Funding Regulation’ (2021) 115 *American Journal of International Law* 34, 37 ff.

¹⁰⁴ This seems to be the case, for example, in the Russian Federation since 2016. In Russia, a model is also practised whereby the funder acquires a minority share in a funded company to secure the funds advanced to this company; if the litigation is successful, the funder can sell its share to the majority shareholder (or even to an adversary). See J Zagonek and P Boulatov, ‘Third-Party Litigation Funding: Overview (Russian Federation)’ Thomson Reuters Practical Law <<https://uk.practicallaw.thomsonreuters.com/w-036-9531?originationContext=knowHow&transitionType=KnowHowItem&contextData=%28sc.DocLink%29>> accessed 4 March 2023.

¹⁰⁵ On the situation in the US, see VA Shannon, ‘Harmonizing Third-party Litigation Funding Regulation’ (2015) 36 *Cardozo Law Review* 861. On the European Union, see A Cordina (2021) *Erasmus Law Review* 270; K Kolb, ‘Die Finanzierung privater Rechtsstreitigkeiten durch Dritte – Aktuelle Entwicklungen in Europa’, (2023) 1 *DisputeResolution* 3.

¹⁰⁶ See Committee on Legal Affairs (rapporteur: A Voss), *Draft Report with recommendations to the Commission on Responsible private funding of litigation of 17 June 2021* (2020/2130(INL)) <www.europarl.europa.eu/doceo/document/JURI-PR-680934_EN.pdf> accessed 15 February 2023; European Parliamentary Research Service (authors: J Saulnier / K Müller / I Koronthalyova), *Responsible private funding of litigation: European added value assessment* (2021) <[www.europarl.europa.eu/RegData/etudes/STUD/2021/662612/EPRS_STU\(2021\)662612_EN.pdf](http://www.europarl.europa.eu/RegData/etudes/STUD/2021/662612/EPRS_STU(2021)662612_EN.pdf)> accessed 15 February 2023; for a very critical account of this report from the perspective of the funding industry, see J Skog, ‘Illusory Truths and Frivolous Claims: Critical Reflections on a Report on Litigation Funding by the European Parliamentary Research Service’, (2022) *Yearbook of Socio-Economic Constitutions* 87. See also the recommendations by Worldthinks, *Consumer Attitudes to Third Party Litigation Funding and its Potential Regulation in the EU* (27 September 2021) <<https://institutelegalreform.com/wp-content/uploads/2021/09/EU-Litigation-Funding-Survey-WEB.pdf>> accessed 15 February 2023.

and a draft directive on 13 September 2022.¹⁰⁷ However, since such an instrument has not yet been adopted by EU legislature, the unharmonized laws of the member states remain applicable (for collective redress, see below para 58).¹⁰⁸ The Model European Rules of Civil Procedure 2020 (ELI / UNIDROIT) expressly endorse the admissibility of third-party funding, clarifying what should actually be self-evident, namely that the arrangement ‘must be in accordance with applicable law and must not provide for inadequate compensation for the funder or enable the funder to exercise any undue influence on the conduct of the proceedings’ (Rule 245(2)). According to the commentary, the drafters of the Model Rules have dealt with the traditional arguments against third party funding, but do not find them convincing. Rather, they hope for ‘a valid means to increase parties’ opportunities to secure fair and efficient access to justice’.¹⁰⁹ In the meantime, a working group of the European Law Institute is also preparing ‘Principles on Third Party Funding of Litigation’; the results are to be presented in 2024.

- 50 Regardless of the degree of regulation and supervision, providers strive to eliminate existing reservations about their business model through self-regulation. The focus is on express commitments to provide information, to maintain confidentiality and capital adequacy, to prevent conflicts of interests and to refrain from undue influence on the conduct of the case or the party’s lawyers. Mention should be made of the Association of Litigation Funders of England and Wales (ALF), which has given itself a Code of Conduct for Litigation Funders very early (current version as of January 2018) and has defined a

¹⁰⁷ European Parliament, *Resolution of 13 September 2022 with recommendations to the Commission on Responsible private funding of litigation* (2020/2130(INL)) <https://www.europarl.europa.eu/doceo/document/TA-9-2022-0308_EN.pdf> accessed 15 February 2023. For accounts of this rather restrictive proposal, see S Augenhöfer and A Dori, ‘The proposed regulation of Third Party Litigation Funding – much ado about nothing?’ (2023) *Zeitschrift für das Privatrecht der Europäischen Union* 198, 204–207; B Gsell / C Meller-Hannich / A Stadler, ‘Prozessfinanzierung in Deutschland vor dem Hintergrund europäischer Regelungsinitiativen’ (2023) 78 *JuristenZeitung* 989.

¹⁰⁸ Reference can be made to recent contributions for example on the current situation in Austria (A Schuschnigg, ‘Prozessfinanzierer als Rechtsfreund?’ [2022] *Österreichische Jurist:innenzeitung* 20), Cyprus (N Kyriakides / I Fisentzou / N Christodoulou, ‘Cyprus: Affordability and Accessibility of the Civil Justice System’ [2021] *Erasmus Law Review* 235, 243–244), Germany (T Kohlmeier, ‘Einblicke in die Praxis der Prozessfinanzierung’ in B Hess [ed], *Europäische Modellregeln für Zivilverfahren – Prozessfinanzierung* [Giesecking 2022] 63; M Lieberknecht, ‘Die materiell-rechtliche Ersatzfähigkeit von Kosten der Prozessfinanzierung’ [2022] *Neue Juristische Wochenschrift* 3318; AK Mayrhofer and B Gsell in M Schmidt-Kessel [n 42] 223, 254–256), Ireland (D Capper [2021] *Erasmus Law Review* 211), Italy (E D’Alessandro, *Perspectives on Third Party Funding in Italy* [Ledizioni 2019]), Netherlands (JL Luiten, *Third party litigation funding: een korte introductie* [Boom Uitgevers 2017]), Spain (D Agulló Agulló, ‘Los contratos de financiación de litigios por terceros [third-party funding] en España’ [2022] *Revista de Derecho Civil* 183). For an older, but still informative study on France, see C Kessedjian (ed), *Le financement de contentieux par un tiers: Third party litigation funding* (Edition Panthéon Assas 2012). For very brief reports of 29 European countries, see L Bench Nieuwveld and V Shannon Sahani (n 96), chapter 11.

¹⁰⁹ For an account of the discussions between the drafters, see R Stürner, ‘The ELI / UNIDROIT Model European Rules of Civil Procedure: An Introduction to Their Basic Conceptions’ (2022) *Rabels Zeitschrift für ausländisches und internationales Privatrecht* 421, 468.

procedure to govern complaints made against its members by funded litigants.¹¹⁰ Meanwhile, also the American Bar Association has outlined ‘Best Practices for Third-Party Litigation Funding’ (August 2020)¹¹¹ and the European Litigation Funders Association has published a Code of Conduct (June 2022).¹¹²

4.1.3.2 Impact of Third-party Funding on the Conduct of Litigation

- 51 Terms and conditions of commercial litigation funders appear to be in need of regulation if they aim at an inadequate share of the profits and/or undue influence on the party’s conduct of the case. It has been noted (recently, for example, in the comment on Rule 245 of the Model European Rules of Civil Procedure 2020 (ELI / UNIDROIT)) that commercial litigation funding raises issues not only from a financial market law perspective, but also from a procedural law perspective.
- 52 The procedural dimension of third-party funding becomes particularly clear against the background of rules that require a party to inform the court and the other party that it has entered into a funding agreement. This is probably the aspect in this context that has attracted most comparative law attention in recent years.¹¹³ Reference is made here again to the solution in the Model European Rules of Civil Procedure 2020 (ELI / UNIDROIT). Rule 245(1) reads: ‘A party who receives funding for the proceedings from a professional third-party funder or from a crowd-funder shall disclose this fact and the identity of the funder to the court and the other party at the commencement of proceedings. The details of such a third-party funding arrangement are, however, not subject to this requirement.’
- 53 Whereas a duty to disclose makes perfect sense in arbitration and collective redress (see below paras 57-62), it seems doubtful whether it is also appropriate in ordinary civil and commercial proceedings before state courts. Most of the reservations that are often expressed in connection with third-party funding (namely the alleged additional burden on the courts or the risk of unfair agreements) must be addressed by legislation and supervisory authorities, but are not relevant for a court that has to decide on a dispute that has already arisen or when it comes to deciding on the distribution of costs.¹¹⁴ Of course,

¹¹⁰ See <<https://associationoflitigationfunders.com/code-of-conduct/documents>> accessed 15 February 2023. For a detailed discussion, see J Barnes, ‘England’ in S Friel (n 7) 23, para 3.8 ff. According to Blackstone’s Civil Practice 2022 (n 10) para 5.15, in practice, courts and tribunals place some weight on this code, despite its voluntary nature.

¹¹¹ See <<https://www.americanbar.org/content/dam/aba/directories/policy/annual-2020/111a-annual-2020.pdf>> accessed 15 February 2023.

¹¹² See <<https://elfassociation.eu/about/code-of-conduct>> accessed 15 February 2023.

¹¹³ Cf V Shannon Sahani (2021) 115 American Journal of International Law 34: ‘the biggest issue with respect to regulating dispute finance that global regulators have begun to address is disclosure’.

¹¹⁴ For the contrary position, see R Stürner (2022) *RechtsZeitschrift für ausländisches und internationales Privatrecht* 421, 468: ‘The judge should not be obliged to decide on the distribution of costs without any knowledge of the contents of such arrangements, thus running the risk of favouring or even subsidizing the execution of dubious cost agreements, at least in cases of profit-oriented financing by the parties’ lawyers or third parties.’

it is always a challenge for a court when one party acts particularly aggressively or refuses to accept settlement proposals which from the judge's perspective seem reasonable. However, such situations can occur in every lawsuit, independent of whether a party is conducting the litigation based on its own financial resources or with the support of a funder. Moreover, the fact that the court or the opponent knows that a party is dependent on external funding even increases the risk of inappropriate settlement proposals: This information creates an incentive that the proposal will not be based on the merits and the prospect of success of the claim, but mainly on the party's financial weakness and on the fact that it is obviously dependent on an early settlement and payment. Against this background, much can be said against a general duty to disclose and for a 'veil of ignorance', following John Rawls' famous theory of justice.

- 54 Another question is how the court should react if the third-party funder interferes too much in the process. The Model European Rules of Civil Procedure 2020 (ELI / UNIDROIT) make it clear that the funding arrangement must not enable the funder to exercise any undue influence on the conduct of the proceedings (Rule 245(2)). Particularly interesting is the sanction foreseen in case this prohibition is violated: According to Rule 245(4), this does not constitute a defence against the claim of the party availing itself of third-party funding. However, having made its decision on the claim, the court may ask for details of fee arrangements with the funder relevant for the instance at stake, and, upon consultation with the parties, it may take into account any disregard of applicable law or lacking fairness of the arrangement when it renders the decision on reimbursement of costs. This solution proposed in the Model Rules is in line, for example, with English and South African law, where the court has discretion to issue a cost order against the funder.¹¹⁵ Probably not least to avoid such liability, the ALF Code of Conduct for Litigation Funders (see above para 50) stipulates that the funder will not seek to influence the funded party's solicitor or barrister to cede control or conduct of the dispute (9.3) and that the agreement shall state whether (and if so how) the funder may provide input to the party's decisions in relation to settlements (11.1).

4.2 Demand Side of Litigation Funding

4.2.1 General Remarks

- 55 It can be assumed that the business model of third-party funding was developed and is still primarily operated for business clients that conduct classic civil and commercial litigation with high amounts in dispute before state courts. For reasons already mentioned, third-party funders typically support claimants (or counter-claimants), and they take care that they support likely winners only. For example, third-party funding gained a lot of attention in Europe in cartel damages litigation brought by prominent companies after the so-called Truck Cartel was uncovered from 2016 onwards. In the case of an

¹¹⁵ UK: Blackstone's Civil Practice 2022 (n 10) para 5.15, 68.65; WH van Boom in WH van Boom (n 14) 5, 18. South Africa: GM Solas (n 13) 81–82.

engagement on the plaintiff's side, the funder benefits through its participation in the litigation recovery; typically, a non-recourse agreement is made: if the plaintiff loses, the funder goes away empty-handed. However, engagement on the defendant side is not completely excluded either, provided that it can be precisely quantified from the outset what the economic value will be for the funded defendant if a claim brought against it is dismissed or a settlement below a certain threshold can be reached.¹¹⁶

- 56 In contrast, it hardly seems attractive for funders to work with individual consumers and this, if at all, only when it comes to consumer plaintiffs who want to enforce substantial monetary claims (especially in personal injury cases). But even from an individual consumer's point of view, it usually does not make sense to look for a funder anyway, but rather to use a service provider that offers an all-round service that completely relieves the client of the hassle of enforcing the law (for such forms of active funding, see below para 74). In the following, two special groups of demanders will be addressed: claimants in collective proceedings and parties to arbitration proceedings.

4.2.1 Collective Proceedings

- 57 Notwithstanding the already mentioned fact that third-party litigation funding is mainly aimed at individual commercial claimants, companies active in this field have also discovered collective redress funding as a business model. Particularly interesting is the situation in Australia, where just such a case tipped the scales in favour of recognising third-party funding as permissible.¹¹⁷ It can even be said that private funding in Australia has since evolved largely through class actions brought on behalf of consumers.¹¹⁸ Similar reports come from Canada,¹¹⁹ while US class actions, traditionally rather facilitated by contingency fee arrangements (see below para 66), is now also described as a growing

¹¹⁶ On such respondent-/defendant-side funding, see the American Bar Association's 'Best Practices for Third-Party Litigation Funding' (<<https://www.americanbar.org/content/dam/aba/directories/policy/annual-2020/111a-annual-2020.pdf>> accessed 15 February 2023) para III.B.6 and V.F: 'defendant-side funding will generally involve situations in which a realistic economic exit point, as well as pricing based upon that exit point, can be determined'. For a detailed analysis, see E Samra, 'The Business of Defense: Defense-Side Litigation Financing' (2016) 83 University of Chicago L. Rev. 2299.

¹¹⁷ *Campbells Cash and Carry Pty Ltd v Fostif Pty Ltd* (High Court of Australia), Judgment 30 August 2006 [2006 HCA 41].

¹¹⁸ See W Chen (n 21) 150 ff; M Legg, 'The Rise and Regulation of Litigation Funding in Australian Class Actions' (2021) Erasmus Law Review 221. For comprehensive treatises and recommendations for law reform, inter alia as regards the regulation of third-party litigation funders, see Australian Law Reform Commission, *Integrity, Fairness and Efficiency – An Inquiry into Class Action Proceedings and Third-Party Litigation Funders* (Final Report, December 2018 <https://www.alrc.gov.au/wp-content/uploads/2019/08/alrc_report_134_webaccess-1.pdf> accessed 15 February 2023), and Parliamentary Joint Committee on Corporations and Financial Services, *Litigation funding and the regulation of the class action industry* (December 2021 <<file:///C:/Users/Wolfgang%20Hau/Downloads/Litigation%20funding%20and%20the%20regulation%20of%20the%20class%20action%20industry%20report.pdf>> accessed 15 February 2023).

¹¹⁹ C Piché, 'Transparency and oversight of class actions funding in Canada' in X Kramer / J Hoevenaars / B Kas / E Themeli (ed), *Frontiers in Civil Justice* (Elgar 2022) 277, 282 ff; GM Solas (n 13) 46–49.

market for third-party funders.¹²⁰ A European example of open-mindedness towards litigation funding in collective proceedings is the ‘Austrian-style class action’: Under this model, a non-profit consumer protection association has the claims of consumers assigned to it and then asserts these bundled claims with a lawsuit; the Austrian courts accept that such class actions are usually brought with the support of a commercial funder.¹²¹

- 58 In contrast to the development described above are the reservations repeatedly expressed about the commercialisation of collective redress, which is widely believed to be associated with the involvement of profit-oriented financiers.¹²² German courts, for example, have considered it inadmissible for a consumer protection association to petition for a collective-interest injunction with the support of a professional funder.¹²³ This does not seem convincing in jurisdictions (such as Germany) where the defendant company is not legally prevented from resorting to commercial funding: in this situation, it is a question of procedural equality of arms to also grant this instrument to the plaintiff’s side (whereby it is of course up to both sides whether they actually succeed in finding a funder).¹²⁴ In addition, it should be borne in mind that it is precisely collective redress that has a very special role in facilitating access to justice, which is why one should not rashly refrain from also using the self-interests of financiers if they are useful to this overriding goal. Consumer protection law without collective redress will remain a dead letter, but the same seems to be true for collective redress without efficient funding.¹²⁵
- 59 In Europe, the discussion is not yet closed.¹²⁶ The openness of the European Model Rules of Civil Procedure 2020 (ELI/UNIDROIT), on the one hand, is reflected in Rule 237(1), which succinctly states that ‘a qualified claimant may use third-party litigation funding’. As a safeguard, Rule 237(2) only provides for a somewhat broader disclosure requirement than the general Rule 245: ‘A court may, however, require a qualified claimant to

¹²⁰ C Morris / A Hill / A Patel, ‘Class actions’ in S Friel (n 7) 287, para 9.103 ff.

¹²¹ Case 60b224/12b (Supreme Court of Justice of Austria), Judgment 27 February 2013 [ECLI:AT:OGH0002:2013:0060OB00224.12B.0227.000].

¹²² For thorough analysis of the viability of such reservations, see I Tillema, ‘Entrepreneurial motives in Dutch collective redress: Adding fuel to a compensation culture?’ in WH van Boom (n 14) 222; more recently: I Tillema, ‘Dutch collective actions and the rise of entrepreneurial actors: Navigating between access to justice and a claim culture’ in X Kramer / J Hoevenaars / B Kas / E Themeli (ed), *Frontiers in Civil Justice* (Elgar 2022) 239.

¹²³ Case IZR 205/17 (Federal Court of Justice of Germany), Judgment 9 May 2019 [ECLI:DE:BGH:2019:090519UIZR205.17.0]. For a critical assessment of the German case-law, see A Stadler in X Kramer / J Hoevenaars / B Kas / E Themeli (ed), *Frontiers in Civil Justice* (Elgar 2022) 260, 266–268.

¹²⁴ See IN Tzankova and XE Kramer, ‘From Injunction and Settlement to Action: Collective Redress and Funding in the Netherlands’ in A Uzelac and S Voet (ed), *Class Actions in Europe: Holy Grail or a Wrong Trail?* (Springer 2021) 97, para 4.1.

¹²⁵ S Voet (n 97) 294.

¹²⁶ Cf A Cordina (2021) Erasmus Law Review 270; XE Kramer and I Tillema, ‘The Funding of Collective Redress by Entrepreneurial Parties: The EU and Dutch Context’ (2020) *Revista Ítalo-Española de Derecho Procesal* 165; S Voet (n 97) 289 ff.

disclose the details of any such funding agreement relevant for the instance at stake to the court and, in so far as appropriate, to the parties.'

- 60 In its Directive 2020/1828 of 25 November 2020 on representative actions for the protection of the collective interests of consumers, the EU could not agree to require the Member States to allow third-party funding. The admissibility thus remains a question of national law, but Art 10 of the Directive makes it clear that at the EU level one has the dangers rather than the advantages in mind.¹²⁷ Furthermore, it is unclear whether Art 12 of the Directive, according to which the loser has to bear the costs, also covers a contingency fee that a party has agreed with a commercial litigation funder.¹²⁸ Against this backdrop, doubts were expressed as to whether the financing of such procedures would prove attractive at all.¹²⁹ The implementation of the Directive in Germany is particularly disappointing. Sec. 4 Verbraucherrecht durchsetzungsgesetz (Consumer Rights Enforcement Act) of 12 October 2023 allows third-party funding of a representative action in principle, but under very strict conditions. It seems reasonable that the representative action is inadmissible if the financier is a competitor of the defendant company or is dependent on the latter. It is also clear that it must be ensured that the financier will not influence the conduct of the proceedings of the body authorised to bring the action, including decisions on settlements, to the detriment of consumers. However, the final blow is dealt by another provision that makes commercial third-party financing de facto impossible: according to this provision, the representative action is inadmissible if the

¹²⁷ Art 10 of the Directive 2020/1828 of 25 November 2020 on representative actions for the protection of the collective interests of consumers reads:

1. Member States shall ensure that, where a representative action for redress measures is funded by a third party, insofar as allowed in accordance with national law, conflicts of interests are prevented and that funding by third parties that have an economic interest in the bringing or the outcome of the representative action for redress measures does not divert the representative action away from the protection of the collective interests of consumers.

2. For the purposes of paragraph 1, Member States shall in particular ensure that:

(a) the decisions of qualified entities in the context of a representative action, including decisions on settlement, are not unduly influenced by a third party in a manner that would be detrimental to the collective interests of the consumers concerned by the representative action;

(b) the representative action is not brought against a defendant that is a competitor of the funding provider or against a defendant on which the funding provider is dependent.

3. Member States shall ensure that courts or administrative authorities in representative actions for redress measures are empowered to assess compliance with paragraphs 1 and 2 in cases where any justified doubts arise with respect to such compliance. To that end, qualified entities shall disclose to the court or administrative authority a financial overview that lists sources of funds used to support the representative action.

For an account of these provisions of the Directive, see S Augenhöfer and A Dori, (2023) *Zeitschrift für das Privatrecht der Europäischen Union* 198, 202–204.

¹²⁸ On this aspect, see A Stadler, 'Prozessfinanzierung und Kostenerstattung' in C Berger / B Boemke / HF Gaul / L Haertlein / B Heiderhoff / E Schilken (ed), *Prozessrecht Zwangsvollstreckungsrecht Insolvenzrecht: Festschrift für Ekkehard Becker-Eberhard* (CH Beck 2022) 553.

¹²⁹ Cf F Gascón Inchausti, 'A new European way to collective redress? Representative actions under Directive 2020/1828 of 25 November' (2021) *Zeitschrift für das Privatrecht der Europäischen Union* 61, 78.

financier is promised an economic share of more than 10 per cent of the amount to be paid by the defendant company.

4.2.2 Arbitration Proceedings

- 61 As a rule, an indigent party does not receive state legal aid for the conduct of arbitration proceedings. Most legal expenses insurance policies also offer no or only limited protection because, according to the terms and conditions, coverage of the costs of arbitration is either excluded altogether or limited to the (regularly significantly lower) costs of state court proceedings. Consequently, access to arbitration will often depend on support from a commercial third-party funder.¹³⁰ In this context, the policy considerations discussed with regard to private funding of state litigation (see above para 2) are of limited relevance. In particular, there is no threat of increased litigation burdening the courts; on the contrary, arbitration is expected to relieve the courts. However, other aspects obviously play a greater role than in litigation, in particular the confidentiality of the arbitration proceedings¹³¹ and the independence of the arbitrators in relation to the third party.
- 62 It is well known that some jurisdictions attach considerable economic importance to their attractiveness as arbitration centres. It is therefore not surprising that legislation in recent times, for example in Hong Kong and Singapore, has opened up the possibility of third-party funding specifically as regards (international) arbitration proceedings.¹³² It seems interesting that in both countries, at least for the time being, third-party funding remains largely prohibited in litigation and in Singapore also in domestic arbitration. Against the background of such national legislation in arbitration hubs, it is not surprising that third-party funding is also increasingly taken into account in the rules of the arbitral institutions. Mention should be made here, for example, of Art 11(7) of the 2021 revision of the ICC Rules,¹³³ which provides that ‘each party must promptly inform the Secretariat, the arbitral tribunal and the other parties, of the existence and identity of any non-party which has entered into an arrangement for the funding of claims or defences and under which it has an economic interest in the outcome of the arbitration’. What is

¹³⁰ For detailed accounts of the various legal and economic aspects, see J von Goeler, *Third-party funding in international arbitration and its impact on procedure* (Wolters Kluwer 2016); J Commission and Y Mohammad, *Third-Party Funding in International Arbitration* (Oxford UP 2022); BM Cremades and A Dimolitsa (ed), *Third-Party Funding in International Arbitration* (Wolters Kluwer 2013); L Bench Nieuwveld and V Shannon Sahani (n 96); N Pitkowitz (ed), *Handbook on Third-Party Funding in International Arbitration* (JurisNet 2018); MF Sweify, *Third Party Funding in International Arbitration: A Critical Appraisal and Pragmatic Proposal* (Edward Elgar 2023).

¹³¹ See S Walsh and Z Krug, ‘Privilege and confidentiality’ in S Friel (n 7) 53, para 5.176 ff.

¹³² Cf Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Ordinance 2017 (Hong Kong) and Code of Practice for Third Party Funding of Arbitration 2019 (Hong Kong); Civil Law (Amendment) Act 2017 (Singapore). For details, see B Zhang (n 96) 55 ff (Hong Kong), 93 ff (Singapore); J Barnes, ‘Australia, Hong Kong, Singapore and global’ in S Friel (n 7) para 3.149 ff (Hong Kong) and para 3.158 (Singapore); GM Solas (n 13) 71–78 (Singapore) and 78–80 (Hong Kong).

¹³³ International Chamber of Commerce, *ICC Arbitration Rules* (2021) <<https://iccwbo.org/dispute-resolution-services/arbitration/rules-of-arbitration>> accessed 15 February 2023.

remarkable about this provision is, on the one hand, that it takes the admissibility of third-party funding for granted and, on the other hand, that the prescribed disclosure is very narrowly defined (information is only to be provided about the identity of the financier and the existence, not the content, of a financing arrangement). Moreover, the fact that the new provision was inserted in Art 11 ICC Rules makes its meaning clear: It is primarily a matter of ensuring the independence of the arbitral tribunal in relation to the funder. Very similar considerations obviously underlie, for example, the 2021 version of the ICDR Rules (Art 14(7))¹³⁴ or The Hague Rules on Business and Human Rights Arbitration of 2019 (Art 55).¹³⁵

5 FINANCING EXISTING DISPUTES: ACTIVE FUNDING

- 63 As mentioned at the outset (see above para 11), passive funding brings the money to the litigation, while active funding brings the litigation to the money.¹³⁶ This can be achieved either by the law firm in charge of the litigation also taking over the pre-financing or by the owner of the disputed claim transferring it to the funder, who then asserts it in its own name in court.

5.1 Pre-financing of the Litigation by Lawyers

5.1.1 Admissibility

- 64 Under the rules of some jurisdictions, lawyers can more or less exempt their clients from the cost risk of litigation: no win, no fee! It can be assumed that such agreements have always been practised all over the world, whether permitted or not.¹³⁷ The situation in the UK, the USA and continental Europe is briefly discussed here.
- 65 In the UK, so-called ‘conditional fee agreements’ (CFAs) are of practical importance, in particular for personal injury and libel claims, but increasingly also in commercial litigation.¹³⁸ Under a CFA, the fee to which the lawyer is only entitled in the event of success is based on the effort expended for litigation plus an additional ‘success fee’.¹³⁹ The success fee uplift is typically in a range between 5 % (when the prospect of success is 95 %) and 150 % (when the prospect of success is 40 %).¹⁴⁰ If the claim is not successful, the client is protected against having to pay their own lawyers. Clients who wish to insure

¹³⁴ International Centre for Dispute Resolution of the American Arbitration Association, *International Dispute Resolution Procedures (Including Mediation and Arbitration Rules)* (2021) <https://go.adr.org/rs/294-SFS-516/images/ICDR_Rules.pdf> assessed 15 February 2023.

¹³⁵ The Hague Rules on Business and Human Rights Arbitration (2019) <https://www.cilc.nl/cms/wp-content/uploads/2019/12/The-Hague-Rules-on-Business-and-Human-Rights-Arbitration_CILC-digital-version.pdf> assessed 15 February 2023.

¹³⁶ For a detailed analysis, see GM Solas (n 13) 138 ff, 146 ff.

¹³⁷ C Hodges / S Vogenauer / M Tulibacka (n 29) 96.

¹³⁸ Blackstone’s Civil Practice 2022 (n 10) para 6.3.

¹³⁹ See Sec 58 Courts and Legal Services Act 1990 (UK).

¹⁴⁰ Blackstone’s Civil Practice 2022 (n 10) para 6.11.

themselves also against claims for reimbursement of costs by prevailing opponents can additionally take out after-the-event insurance (see above para 45). It should be noted, however, that CFAs do not protect the client against winning the case but then having to pay such substantial fees to the own lawyers that the success is devalued. This is significant in the UK because, under the influence of the Jackson Report,¹⁴¹ the legislature has directed that, in principle, the success fee may not be recovered against the losing opponent.¹⁴² It should also be mentioned that the CFA does not normally cover expert costs or other disbursements of the lawyer which have to be borne by the client.¹⁴³

- 66 Under the contingency fee model typical of the USA, the successful lawyer is remunerated in the form of a percentage share of the winnings in the case, the so-called *quota pars litis*.¹⁴⁴ Under such agreements, the client is protected both from any costs in the event of a defeat and from fees that reach or possibly even exceed the profit in the event of a victory. Incidentally, in this model the lawyer is interested in reaching a big judgment or settlement, not in adding up as many billable hours as possible.¹⁴⁵
- 67 While legal systems in continental Europe have traditionally had strong reservations about success-based lawyers' fees,¹⁴⁶ today it seems difficult to find a uniform line of approach. The European Model Rules of Civil Procedure 2020 (ELI/UNIDROIT) make a legal policy statement rather than a description of the applicable law when Rule 245(3) succinctly states that 'parties may enter into success fee arrangements with counsel or a third-party funder', as long as such arrangements are 'consistent with applicable law, the parties' access to fair legal representation and the integrity of the proceedings'.¹⁴⁷ A differentiating position is taken by the Council of Bars & Law Societies of Europe (CCBE), which states in Art 3.3.1 of its Code of conduct for European lawyers that 'a lawyer shall

¹⁴¹ See R Jackson (n 34) 125 ff.

¹⁴² Sec 58A(6) Courts and Legal Services Act 1990 (UK), as substituted by Sec 44 Legal Aid, Sentencing and Punishment of Offenders Act 2012 (UK). For the discussion on the abolishment of the recoverability of success fees, see C Hodges (n 9) 141 ff., 281. See also J Peysner, *Access to Justice: A Critical Analysis of Recoverable Conditional Fees and No Win No Fee Funding* (Palgrave 2014).

¹⁴³ See B Summerfield and E Shafon, 'Contingency and conditional fee agreements' in S Friel (n 7) 237, para 8.96; Blackstone's Civil Practice 2022 (n 10) para 5.6.

¹⁴⁴ A similar arrangement is meanwhile also known in the UK: for so-called damages-based agreements (DBAs), see Sec 58AA Courts and Legal Services Act 1990 (UK); Blackstone's Civil Practice 2022 (n 10) para 5.16–5.17. R Mallalieu, 'Funding Litigation' in P Hurst / S Middleton / R Mallalieu, *Costs & Funding following the Civil Justice Reforms* (Thomson Reuters, 6th ed 2020) para 2–22 ff.

¹⁴⁵ Cf J De Mot / M Faure / L Visscher (n 67) 45–46.

¹⁴⁶ For an earlier comparative overview, see, for example, M Faure / F Fernhout / N Philipsen, 'No Cure, No Pay and Contingency Fees' in M Tuil and L Visscher (n 2) 33, 41–51. In contrast, the current position in Russia as regards contingency fee arrangements between qualified advocates and their clients seems to be extremely liberal; see J Zagonek and P Boulatov, 'Third-Party Litigation Funding: Overview (Russian Federation)' Thomson Reuters Practical Law <<https://uk.practicallaw.thomsonreuters.com/w-036-9531?originationContext=knowHow&transitionType=KnowHowItem&contextData=%28sc.Do-clink%29>> accessed 4 March 2023.

¹⁴⁷ This is said to apply both in conventional and in collective proceedings: Rule 245(5). According to Rule 245(4), a violation of the requirements of Rule 245(3) has the same effects as a violation of the provisions on third-party funding (see above para 54).

not be entitled to make a *pactum de quota litis*’ (as defined in Art 3.3.2 as ‘an agreement between a lawyer and the client entered into prior to final conclusion of a matter to which the client is a party, by virtue of which the client undertakes to pay the lawyer a share of the result regardless of whether this is represented by a sum of money or by any other benefit achieved by the client upon the conclusion of the matter’).¹⁴⁸ Behind this, as the commentary on Art 3.3 explains, is the conviction that ‘an unregulated agreement for contingency fees (*pactum de quota litis*) is contrary to the proper administration of justice because it encourages speculative litigation and is liable to be abused’. At the same time, however, it is also emphasised that it is not ‘intended to prevent the maintenance or introduction of arrangements under which lawyers are paid according to results or only if the action or matter is successful, provided that these arrangements are under sufficient regulation and control for the protection of the client and the proper administration of justice’.

- 68 It becomes apparent that many legislators are in principle still committed to traditional concepts of professional order, but on the other hand want to ensure access to justice and predictability of legal costs. France still expressly prohibits a *quota litis*, but allows a success-based fee component, which in practice is often agreed as a bonus in addition to a fixed fee.¹⁴⁹ Under the new German rules,¹⁵⁰ agreements according to which the remuneration or the amount of the fee depends on the outcome of the proceedings or under which the lawyer retains a part of the award made by the court as a fee are possible if the mandate relates to a monetary claim of no more than EUR 2,000 or if the client would be deterred from taking legal proceedings in the absence of such an agreement upon a reasonable assessment of the facts of the case (but irrespective of the client's financial circumstances). An agreement which provides that in the event of failure no remuneration or a lower remuneration than the statutory remuneration is to be paid is only permitted if it is also agreed that in case of success an appropriate surcharge on the statutory remuneration will be paid. Even in the constellations just mentioned, in which a success fee is possible, lawyers in court proceedings are still prohibited from promising their clients to pay other costs (ie, court costs or costs to be reimbursed to the prevailing opponent). And finally, it also seems remarkable that even to the extent that a success fee or another form of litigation financing by law firms is legally permitted,

¹⁴⁸ Council of Bars & Law Societies of Europe, *Charter of core principles of the European legal profession & Code of conduct for European lawyers* (2019) <https://www.ccbe.eu/fileadmin/speciality_distribution/public/documents/DEONTOLOGY/DEON_CoC/EN_DEON_CoC.pdf> accessed 15 February 2023.

¹⁴⁹ See Art 11(3) *Règlement Intérieur National de la Profession d'Avocat* (National Rules of Procedure for the Legal Profession).

¹⁵⁰ See Sec 49b(2) *Bundesrechtsanwaltsordnung* (Federal Lawyers' Act) and Sec 4a *Rechtsanwaltsvergütungsgesetz* (Act on the Remuneration of Lawyers), both as amended by law of 10 August 2021. For details, see AK Mayrhofer and B Gsell in M Schmidt-Kessel (n 42) 223, 250–252.

the traditional self-image of the legal profession can lead to such opportunities not being utilised.¹⁵¹

5.1.2 Fields of Application and Problems in Practice

- 69 Although in principle available for both sides,¹⁵² what all models of success-oriented remuneration have in common is that they are typically target alleged creditors (which means, at least normally, claimants) rather than alleged debtors (defendants). The decisive factor for this instrument of private funding is not whether the client is a company or an individual, but that the claim is so high and its success so likely that it is worth the lawyer's while. Therefore, vulnerable litigations such as consumers or tort victims can also benefit if the lawyer manages to bundle a sufficient number of individual claims in a collective action.¹⁵³ This also explains why the European Law Institute expressly advocates the admissibility of contingency fees as a necessary complement to legal aid in the context of human rights litigation.¹⁵⁴ At the same time, this allows the lawyers' and evidence costs for the individual claim to be significantly reduced, which facilitates access to justice.
- 70 The criticism often levelled against contingency fees, namely that lawyers who are not remunerated according to their time and effort have more of an incentive to advise their clients to settle prematurely and thus disadvantageously, seems convincing at first glance, but does not appear correct in this generality.¹⁵⁵ In contrast, pre-financing by lawyers is obviously not suitable for individual parties if their claims cannot be bundled with other claims for legal or factual reasons and if, from the lawyers' point of view, isolated enforcement is either too risky or has too little prospect of a big judgment or settlement. This appears problematic if the non-acceptance of a mandate is simply based on the fact that it concerns a claim whose amount is significant for the client, but not for the lawyers. On the other hand, it actually seems sensible for the administration of justice that lawyers examine the prospects of success of claims presented to them more critically from the outset than in the case of a classic effort-based remuneration,

¹⁵¹ For a report on a survey of German law firms in this regard, see M Kilian, 'Der Rechtsanwalt als Kostenfinanzierer – Wenig Bereitschaft zur Kostenfinanzierung über das Erfolgshonorar hinaus' (2023) *Anwaltsblatt* 424.

¹⁵² See, for example, Blackstone's Civil Practice 2022 (n 10) para 6.3; B Summerfield and E Shafon (n 143) para 8.94, 8.114 and 8.117.

¹⁵³ On the importance of success-based remuneration of lawyers for the viability of collective redress, but also on potential conflicts of interest between the lawyers and the class, see S Voet (n 97) 273 ff.; S Keske / A Renda / R Van den Bergh, 'Financing and Group Litigation' in M Tuil and L Visscher (n 2) 57, 73 ff.

¹⁵⁴ European Law Institute, *Business and Human Rights: Access to Justice and Effective Remedies (with input from the European Union Agency for Fundamental Rights, FRA)* (2022) para 2.6.6 <https://www.europeanlawinstitute.eu/fileadmin/user_upload/p_eli/Publications/ELI_Report_on_Business_and_Human_Rights.pdf> accessed 15 February 2023.

¹⁵⁵ On approaches to empirically investigate this controversial hypothesis, see J De Mot / M Faure / L Visscher (n 67) 48–49.

which tends to tempt them to also advise the filing of rather questionable lawsuits.¹⁵⁶ The crucial question is actually not whether success fees lead to more or rather less litigation or whether they are suitable for every case and client, but whether they can help to ensure that more lawsuits can be brought that deserve it.¹⁵⁷

Lawyers offering success-oriented remuneration also resort to insurance to protect themselves against the financial risk of losing a case.¹⁵⁸ Apart from this unsurprising observation, at least in principle, one could assume that lawyers and passive litigation funders see themselves as competitors. In fact, however, their services tend to complement each other, especially when clients combine conditional fee agreements with after-the-event insurance in order to secure themselves as much as possible (see above para 65). In practice there is also direct cooperation between law firms and third-party funders,¹⁵⁹ but this can raise difficult professional ethics issues for lawyers (for example, with regard to the prohibition of fee splitting).¹⁶⁰ On the other hand, in those jurisdictions where the prohibition of contingency fees or other forms of litigation funding by lawyers is still strictly enforced, the question arises as to whether lawyers and law firms may also be prohibited from participating economically in litigation funding companies.¹⁶¹

5.2 Transfer of the Claim

- 71 It seems worth noting that the transfer of claims as a financing option has so far received significantly less attention from a comparative perspective than passive funding or the admissibility of contingency fees.¹⁶² The transfer model involves the assignment of a disputed claim to a private individual or company by the holder of the claim who does not have the means to enforce it in court or wishes to avoid the hassle involved. The funder/assignee can then sue the alleged debtor in its own name, either at its own expense or again with the assistance of a financier. It should be noted, however, that legal

¹⁵⁶ On this filter effect or 'gatekeeper function' of lawyers, see J De Mot / M Faure / L Visscher (n 67) 46–47; L Visscher and T Schepens in M Tuil and L Visscher (n 2) 18–19. Economic research suggests that in this respect contingency fees are also superior to third-party funding, cf B Deffains and C Desrieux (2015) 43 *International Review of Law and Economics* 178, 186–188.

¹⁵⁷ Cf M Faure / F Fernhout / N Philipsen in M Tuil and L Visscher (n 2) 39–41.

¹⁵⁸ C Toms (n 10) para 8.63, 8.83 ff.

¹⁵⁹ See American Bar Association's 'Best Practices for Third-Party Litigation Funding' (<<https://www.americanbar.org/content/dam/aba/directories/policy/annual-2020/111a-annual-2020.pdf>> accessed 15 February 2023) para III.A/B: direct lawyer-funder arrangements as opposed to client-funder arrangements. For details, see: GM Solas (n 13) 144, 155 ff.

¹⁶⁰ American Bar Association's 'Best Practices for Third-Party Litigation Funding' (<<https://www.americanbar.org/content/dam/aba/directories/policy/annual-2020/111a-annual-2020.pdf>> accessed 15 February 2023) para III.A.1; B Summerfield and E Shafton (n 143) para 8.119–8.120 and 8.126.

¹⁶¹ For a recent account from an Austrian perspective, see L Prodingner, 'Die Beteiligung von Rechtsanwälten an gewerblichen Prozesskostenfinanzierungsgesellschaften: Der Reiz des Geldes im Fall des Prozessersfolgs' in Garber T (ed), *Festschrift Matthias Neumayr* (Manz 2023) 1337.

¹⁶² Reference should be made, however, to a recent comparative study of Swiss, German and Austrian law: A Heisch, *Abtretungsmodelle im Zivilprozess – Die gebündelte Anspruchsdurchsetzung mittels Inkassozession, objektiver Klagenhäufung und Prozessfinanzierung* (Schulthess 2022).

expenses insurance does not usually cover assigned claims and that public funding might neither be available following an assignment.¹⁶³

- 72 In the case of active funding, the client/assignor should always be relieved of the litigation,¹⁶⁴ but two variants must be distinguished, depending on the distribution of the risk of success. If the funder bears this risk, the client immediately receives a price in return for the assigned claim, but this price is significantly lower than the nominal value of the claim.¹⁶⁵ If, on the other hand, the risk of success remains with the client, he or she will only receive money from the financier if the latter has won the case against the debtor. In this variant, the focus is on law enforcement as a service, not on a classic sale of the claim. Which model is chosen depends first on the legal admissibility of the assignment (see below para 75) and then on the client's preferences. For indigent creditors who are dependent on 'quick money', the first option will be of particular interest. In contrast, both models can be considered for economically strong creditors who are primarily interested in being able to concentrate their resources on their core business rather than on litigation.¹⁶⁶
- 73 For the provider side, the motivation to get involved depends above all on whether the number of claims is as large as possible and the claims as uniform as possible, which can be processed with as little effort as possible using legal tech. Against this backdrop, active funding seems particularly important for the enforcement of consumer claims. As already mentioned, collective actions are common in some jurisdictions, where consumer protection organisations pool the claims of as many individual consumers as possible and then sue them in bundles against the company, whereby they are financed by third-party funders (see above paras 57 et seq). Another conceivable area of application for active funding is the enforcement of claims for antitrust damages or other mass torts, which are assigned to a special-purpose vehicle for litigation.¹⁶⁷
- 74 Active funding also plays a major role for individual consumers (or small and medium-sized enterprises) outside of collective redress. This involves working with service providers that are easily accessible, preferably via the internet, and offer an all-round service that completely relieves their clients of the hassle of enforcing their claims.¹⁶⁸ According to the contract, the service provider can, if necessary, also take care of hiring

¹⁶³ Cf, for example, Blackstone's Civil Practice 2022 (n 10) para 5.18.

¹⁶⁴ No active, but normal passive funding takes place when the client transfers the claim to the funder merely as collateral but remains responsible for enforcing the claim against the alleged debtor.

¹⁶⁵ Cf WH van Boom in WH van Boom (n 14) 5, 9; M Reimann (n 6) 47–48.

¹⁶⁶ GM Solas (n 13) 150–152.

¹⁶⁷ See A Stadler, 'Funding of mass claims in Germany: Caught between a rock and a hard place?' in WH van Boom (n 14) 201, 203 ff; A Stadler in L Cadet / B Hess / M Requejo Isidro (n 15) 209, 218 ff; A Pinna, 'Financing Civil Litigation: The Case for the Assignment and Securitization of Liability Claims' in M Tuil and L Visscher (n 2) 109, 110; GM Solas (n 13) 148–150.

¹⁶⁸ For details, see R Caponi and JT Nowak, 'Access to Justice', in B Hess and S Law (ed), *Luxembourg Report on European Procedural Law, Volume II: Implementing EU Consumer Rights by National Procedural Law* (CH Beck Hard Nomos 2019) 63, para 97 ff.

lawyers and experts or negotiating a settlement.¹⁶⁹ With such collection models, from the consumer's point of view it is typically not significant (and often even unclear) whether a genuine assignment takes place or whether he or she remains the creditor. What seems to be more important for the consumer, regardless of the legal construction, is that he or she regularly has to give up a significant part of the expected profit to the service provider. This is no cause for great concern for the consumer or the legal system as long as the claim is rather small and the consumer would not have enforced it in his or her own name. A typical example of this is the lump-sum compensation for the mere hassle associated with flight delays or cancellations:¹⁷⁰ This enables a low-threshold access to justice, admittedly to a doubtful sort of 'justice' that in many cases seems dispensable anyway. The situation is entirely different, however, if the consumer has suffered a real loss but, in the end, even if the defendant company pays what it owes, only receives an amount that is significantly less than the loss because of the service provider's share.¹⁷¹ Access to justice and enforcement of the consumer's claim remains limited in such cases, although this seems particularly noteworthy in those jurisdictions where the litigation loser normally has to bear the entire costs.

- 75 The reservations traditionally expressed against passive funding, which are mostly related to the idea that the funder inappropriately interferes in another party's litigation and possibly even controls the litigation of a party (see above para 54), are at least less relevant in active funding if the funder becomes the owner of the disputed claim. The model, however, stands or falls with the question of whether or under what conditions a legal system permits the assignment of a claim.¹⁷² There are still considerable differences, in particular as regards the admissibility of an assignment for the purpose of litigation or debt collection or an assignment of the right to sue only. Some legal systems expressly prohibit the assignment of claims to lawyers while others restrict the assignment of contested or already pending claims or differentiate between contractual and tort claims. Another common regulatory approach is to subject debt collectors to state licensing and supervision. Against this background, there are ongoing discussions about coherent regulatory frameworks for the activities of special-purpose vehicles,¹⁷³ for

¹⁶⁹ On problems related to this, see R Caponi and JT Nowak (n 168) para 102.

¹⁷⁰ In Europe, for example, such claims can be based on the Regulation establishing common rules on compensation and assistance to passengers in the event of denied boarding and of cancellation or long delay of flights, 261/2004 of 11 February 2004 (EC).

¹⁷¹ On this aspect of under-enforcement of consumer law, see R Caponi and JT Nowak (n 168) 63, para 101.

¹⁷² For comparative overviews over the legality of assignments in the context of litigation funding, see A Pinna in M Tuil and L Visscher (n 2) 113 ff; WH van Boom in WH van Boom (n 14) 5, 12 ff; M Reimann (n 6) 47; G M Solas (n 13) 146–148.

¹⁷³ A Stadler in WH van Boom (n 14) 201, 213 ff; A Stadler in L Cadiet / B Hess / M Requejo Isidro (n 15) 209, 225 ff.

internet platforms active in the field of consumer claims enforcement¹⁷⁴ and for an appropriate market regime for assigned claims.¹⁷⁵

6 ALTRUISTIC FUNDING

- 76 Altruistic forms of funding from the private sector have already been addressed in the context of membership in solidarity groups as a provision for future civil litigation (see above para 13), but can also help an indigent party after a dispute has already arisen.¹⁷⁶ In such cases, it happens that family members or friends grant an interest-free loan to finance the legal costs.¹⁷⁷ Furthermore, charitable organisations offer money or, more often, at least free advice to parties who cannot afford a lawyer.¹⁷⁸ With regard to this, however, the boundaries between private and public funding can be blurred. This is particularly evident in the US, where the Legal Services Corporation ('America's Partner for Equal Justice'),¹⁷⁹ an independent non-profit corporation established by Congress in 1974, distributes its funds to more than hundred independent non-profit legal aid programmes. In this context, so-called 'contingent legal aid funds' (CLAFs), which have been created in various common law jurisdictions, should also be mentioned: This refers to non-profit schemes that originate from a government initiative and fund litigation for eligible claimants or cases in the public interest based on recoveries from previous successful litigation.¹⁸⁰
- 77 Of particular practical importance in the context of altruistic private funding are law firms that provide representation or their expertise free of charge, regardless of the party's success (on contingency fee arrangements, see above paras 64 et seq). In some jurisdictions, so-called *pro bono publico* work is good practice or even required by professional law.¹⁸¹ A well-known example is Rule 6.1 of the Model Rules of Professional Conduct (American Bar Association), which sets out in detail the scope of 'professional responsibility to provide legal services to those unable to pay'.¹⁸² In other countries, however, such altruism is only permissible under strict conditions. For example, German lawyers must give initial out-of-court advice to needy parties for a token amount set by law

¹⁷⁴ Cf R Caponi and JT Nowak (n 168) para 104.

¹⁷⁵ Cf A Pinna in M Tuil and L Visscher (n 2) 122 ff.

¹⁷⁶ For an overview, see R Nayer and R Ahmed, 'Pro bono, philanthropic, charitable and 'revenge' funding' in S Friel (n 7) 217.

¹⁷⁷ Cf C Hodges (n 9) 135.

¹⁷⁸ For the UK, see C Hodges (n 9) 202–205.

¹⁷⁹ For more information, visit the homepage of the Legal Services Corporation: <www.lsc.gov> accessed 15 February 2023.

¹⁸⁰ For details and example from various jurisdictions, see R Nayer and R Ahmed, 'State funding' in S Friel (n 7) 207, para 8.14–8.26; S Voet (n 97) 278 ff.

¹⁸¹ For comparative remarks on lawyers' pro bono work, see M Reimann (n 6) 38–39; R Nayer and R Ahmed, 'Pro bono, philanthropic, charitable and "revenge" funding' in S Friel (n 7) para 8.27–8.43; P Yates, 'CourtNav and Pro Bono in an Age of Austerity' in E Palmer / T Cornford / A Guinchard / Y Marique, *Access to Justice – Beyond the Politics and Policies of Austerity* (Hart 2018) 249.

¹⁸² See <https://www.americanbar.org/groups/professional_responsibility/resources> accessed 15 February 2023.

and participate in free advisory services organised by the bar association;¹⁸³ but an agreement to give comprehensive advice to the party or even to represent the party in court for free or for less than the fees provided by law would be unlawful.¹⁸⁴

- 78 Apart from lawyers, help in litigation to needy parties is also offered by legal laypersons who thus have no general right of audience in court. A well-known example is a ‘McKenzie friend’¹⁸⁵ who ‘quietly assists’ a litigant in person in court proceedings. While in some jurisdictions (eg, Scotland) this work must be done free of charge, in other jurisdictions (eg, England and Wales) McKenzie friends are allowed to work for a fee, but then they regularly have professional indemnity insurance.¹⁸⁶
- 79 Finally, individuals and non-profit organisations that provide funding for lawsuits that can serve as test cases for their causes should also be mentioned here.¹⁸⁷ This can happen in the field of human rights litigation (a well-known example is the American Civil Liberties Union, which has been active in this field for more than 100 years¹⁸⁸), but also in the context of private law (especially in relation to anti-discrimination law or family law issues). Crowdfunding campaigns are likely to become increasingly important;¹⁸⁹ it seems remarkable that the Directive 2020/1828 of 25 November 2020 on representative actions for the protection of the collective interests of consumers (see Recital 52) as well as the Model European Rules of Civil Procedure 2020 (ELI / UNIDROIT) (see Rule 245(1)) expressly mention crowd-funding as an alternative to professional third-party funding. Altruistic fundraising can be organised either on an institutionalised basis or spontaneously, eg, following (social) media reports about the lawsuit of a party in need. Finally, it should be noted that financing another's lawsuit, even if done gratuitously, is not necessarily entirely altruistic: This is how ‘revenge funding’ sometimes occurs, ie, civil lawsuits

¹⁸³ Sec 49a Bundesrechtsanwaltsordnung (Federal Lawyers' Act) (Germany).

¹⁸⁴ Sec 49b(1) Bundesrechtsanwaltsordnung (Federal Lawyers' Act) (Germany). For details, see AK Mayrhofer and B Gsell in M Schmidt-Kessel (n 42) 223, 249.

¹⁸⁵ *McKenzie v McKenzie* (Court of Appeal, UK), Judgment 10 July 1970, [1970] 3 WLR 472. See Lord Chief Justice of England and Wales, *Reforming the courts' approach to McKenzie Friends – Consultation Response* (2019) <<https://www.judiciary.uk/wp-content/uploads/2016/02/MF-Consultation-LCJ-Response-Final-Feb-2019.pdf>> accessed 15 February 2023; Blackstone's Civil Practice 2022 (n 10) para 61.30 ff.

¹⁸⁶ For more information, visit the homepage of the Society of Professional McKenzie Friends: <www.mckenziefriends.directory> accessed 15 February 2023.

¹⁸⁷ See R Nayer and R Ahmed, ‘Pro bono, philanthropic, charitable and “revenge” funding’ in S Friel (n 7) para 8.44–8.51; American Bar Association's ‘Best Practices for Third-Party Litigation Funding’ (<<https://www.americanbar.org/content/dam/aba/directories/policy/annual-2020/111a-annual-2020.pdf>> accessed 15 February 2023) para III.B.4 and V.D.

¹⁸⁸ For more information, visit the homepage of the American Civil Liberties Union: <www.aclu.org> accessed 15 February 2023. See also DL Rhode, *Access to Justice* (Oxford UP 2004) 66.

¹⁸⁹ On this phenomenon, see R Nayer and R Ahmed, ‘Pro bono, philanthropic, charitable and “revenge” funding’ in S Friel (n 7) para 8.45. R Perry, ‘Crowdfunding Civil Justice’ (2018) 59 Boston College Law Review 1357.

financed by someone who has no interest in the subject matter of the dispute, but does have an interest in harming the defendant.¹⁹⁰

¹⁹⁰ Cf the American Bar Association's 'Best Practices for Third-Party Litigation Funding' (<<https://www.americanbar.org/content/dam/aba/directories/policy/annual-2020/111a-annual-2020.pdf>> accessed 15 February 2023) para III.B.5 and V.E. For an exceptional but much discussed example, see N K Chipi, 'Eat Your Vitamins and Say Your Prayers: Bollea v. Gawker, Revenge Litigation Funding, and the Fate of the Fourth Estate' (2017) 72 U. Miami L. Rev 269 (criticising third-party litigation funding as a means of attacking free press). A more recent, but no less spectacular example is reported by B Weiser and C Savage, 'LinkedIn's Co-Founder Helped Fund the Suit Accusing Trump of Rape: Reid Hoffman, a billionaire and critic of Donald J. Trump, is backing E. Jean Carroll's suit against the former president' New York Times of 13 April 2023.

ABBREVIATIONS AND ACRONYMS

Art	Article/Articles
CEPEJ	<i>Conseil de l'Europe Commission européenne pour l'efficacité de la justice</i> (Council of Europe European Commission for the efficiency of justice)
cf	<i>confer</i> (compare)
ch	chapter
CJEU	Court of Justice of the European Union
edn	edition/editions
ed	editor/editors
etc	et cetera
ECLI	European Case Law Identifier
eg	<i>exempli gratia</i> (for example)
ELI	European Law Institute
et seq	et sequens (and the following)
EU	European Union
EUR	Euro
ff	following
fn	footnote (external)
ibid	<i>ibidem</i> (in the same place)
ie	<i>id est</i> (that is)
n	footnote (internal)
no	number/numbers
para	paragraph/paragraphs
Sec	Section/Sections
UK	United Kingdom
UNIDROIT	<i>Institut international pour l'unification du droit privé</i> (International Institute for the Unification of Private Law)
UP	University Press
US / USA	United States of America
v	versus
vol	volume/volumes

LEGISLATION

International/Supranational

Directive 87/344/EEC of 22 June 1987 on the coordination of laws, regulations and administrative provisions relating to legal expenses insurance

Directive of 25 November 2009 on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II)

Directive 2020/1828 of 25 November 2020 on representative actions for the protection of the collective interests of consumers

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International Centre for Dispute Resolution of the American Arbitration Association, International Dispute Resolution Procedures (Including Mediation and Arbitration Rules) (2021) <https://go.adr.org/rs/294-SFS-516/images/ICDR_Rules.pdf> assessed 15 February 2023.

The Hague Rules on Business and Human Rights Arbitration (2019)

National

Arbitration and Mediation Legislation (Third Party Funding) (Amendment) Ordinance 2017 (Hong Kong)

Bundesrechtsanwaltsordnung (Federal Lawyers' Act) (Germany)

Bürgerliches Gesetzbuch (Civil Code) (Germany)

Civil Law (Amendment) Act 2017 (Singapore)

Code des Assurances (Insurance Code) (France)

Code of Practice for Third Party Funding of Arbitration 2019 (Hong Kong)

Courts and Legal Services Act 1990 (UK)

Gesetz über den Versicherungsvertrag (Insurance Contract Act) (Germany)

Legal Aid, Sentencing and Punishment of Offenders Act 2012 (UK)

Rechtsanwaltsvergütungsgesetz (Act on the Remuneration of Lawyers) (Germany)

Verbraucherrecht durchsetzungsgesetz (Consumer Rights Enforcement Act) (Germany)

Model Rules

Model European Rules of Civil Procedure 2020 (ELI / UNIDROIT)

Principles of European Insurance Contract Law 2015 (Project Group “Restatement of European Insurance Contract Law”)

CASES

International/Supranational

Erhard Eschig v UNIQA Sachversicherung AG, Case C-199/08 (CJEU), Judgment 10 September 2009 [ECLI:EU:C:2009:538]

Jan Sneller v DAS Nederlandse Rechtsbijstand Verzekeringsmaatschappij NV, Case C-442/12 (CJEU), Judgment 7 November 2013 [ECLI:EU:C:2013:717]

Pascal Nobile v DAS Rechtsschutz-Versicherungs AG, Case E-21/16 (EFTA Court) Judgment 27 October 2017

National

McKenzie v McKenzie (Court of Appeal, UK), Judgment 10 July 1970 [3 WLR 472]

Campbells Cash and Carry Pty Ltd v Fostif Pty Ltd (High Court of Australia), Judgment 30 August 2006 [2006 HCA 41]

Case 6Ob224/12b (Supreme Court of Justice of Austria), Judgment 27 February 2013 [ECLI:AT:OGH0002:2013:0060OB00224.12B.0227.000]

Case I ZR 205/17 (Federal Court of Justice of Germany), Judgment 9 May 2019 [ECLI:DE:BGH:2019:090519UIZR205.17.0]

Case IV ZR 279/17 (Federal Court of Justice of Germany), Judgment 14 August 2019 [ECLI:DE:BGH:2019:140819UIVZR279.17.0]

Travelers Insurance Company Ltd v XYZ (Supreme Court, UK), Judgment 30 October 2019 [2019 UKSC 48]

Case IV ZR 221/19 (Federal Court of Justice of Germany), Judgment 31 March 2021 [ECLI:DE:BGH:2021:310321UIVZR.221.19.0]

R (on the application of PACCAR Inc and others) v Competition Appeal Tribunal (Supreme Court, UK), Judgment 26 July 2023 [2023 UKSC 28]

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