Nick
Hoffman

Lachlan
Greig

The future for litigation funding in the Cayman Islands

The business of third party funding of litigation is thriving in many of the world's onshore jurisdictions. A recent decision of the Grand Court has opened the door to litigation funding in the Cayman Islands. Cayman is now poised to be among the first of the offshore jurisdictions to welcome the litigation funding industry and benefit from the opportunities it brings.

The business of third party funding of litigation

An increased demand for alternative ways to fund litigation has seen corresponding phenomenal growth in existing litigation funding markets such as England, the United States and Australia, and also the formation of new markets in Asia, the Middle East and Latin America.

Once upon a time, the third party funding market catered only for the funding of impecunious claimants, who otherwise lacked the resources to pursue meritorious claims. Third party funding in this context achieved the public policy objective of enhancing access to justice and was generally accepted as desirable for that reason.

In the past few years, a new type of consumer has entered the market – businesses that are capable of funding their own claims but who are looking for innovative ways to manage the costs (and concomitant risks) associated with litigation – driving a sharp increase in the demand for outside or third party funding. There are perhaps obvious reasons why, from a financial standpoint, businesses engaged in litigation would consider assigning the expense elsewhere: where an entity self-funds the conduct of the claim, its expenses increase and resources are diverted away from the business's core projects. This reduces profitability, both in the short and long term, and lowers the market value of the business. Any proceeds from a successful outcome in the litigation are a "one off" from an accounting perspective and, other than the increase to the entity's cash balance, does not offset the lost profitability caused by slowed growth in core activities. With the benefit of external funding, it is business as usual. Although the business shares any proceeds of the litigation with the funder, the funding arrangement enables the business to generate a gain at no cost. Third party funding arrangements also shift the risks associated with litigation from the claimant to the funder.

Australia, the United States and the United Kingdom have well-developed and sophisticated markets for litigation funding serviced by professional litigation funders. Hong Kong and Singapore recently changed their laws to permit third-party funding in arbitration (although not yet in litigation). In recent cases in Bermuda and Jersey, the courts have approved third-party funding in the absence of legislative intervention, a judicial recognition of the modern tide. While yet to be tested in the British Virgin Islands, judicial obiter suggests a favorable approach to appropriately formulated third-party litigation agreements there too.

Alternative litigation funding in the Cayman Islands

Like many other common law jurisdictions, the Cayman Islands recognizes the English law torts of champerty and maintenance. The origins of these torts are ancient and developed at a time where the legal system lacked due process, and the judiciary lacked independence, facilitating the use of legal process as a tool of oppression by the wealthy. Maintenance is the act of giving assistance or encouragement to a party to litigation by a person who has no interest in the outcome, or any motive recognized by law as justifying such interference. Champerty is an aggravated form of maintenance because the assistance or encouragement is given in exchange for a share in the proceeds of the litigation.

The objectives that these torts sought to achieve in medieval England – to prevent corruption of public justice and preserve the integrity of the litigation process – are no less valid, admirable and relevant today. Of course, the modern legal environment has evolved significantly from that of medieval England. We are fortunate enough to have a talented and independent judiciary administering our laws and a democratically elected legislature capable of passing new law where the old laws fall short. The torts of champerty and maintenance are, in today's environment, the metaphorical sledgehammer cracking the nut. Despite this, the torts remain in (almost) full force and effect in the Cayman Islands and fetter the ability of modern day litigants to access alternative forms of litigation funding.

Broadly, if a claimant is not self-funded, there are two potential alternative sources of funding for the conduct of the claim; a third party or the attorney acting for the claimant. The attorney "funds" the conduct of the claim in the sense that payment of the attorney's fees is deferred until, and conditional upon, the outcome of the claim and thereby relieves the claimant of the burden of paying legal fees throughout the conduct of the claim (or at all).

A series of decisions by the Grand Court in recent years have made inroads in the context of litigation funding by attorneys in the form of "conditional" fee agreements (i.e., an agreement by which a Cayman Islands attorney is paid his usual fee, plus an agreed uplift calculated as a percentage of that fee, if the plaintiff is successful, and is paid nothing if the plaintiff is unsuccessful). The Cayman courts have sanctioned a number of conditional fee agreements between Cayman Islands attorneys and impecunious plaintiffs who could not otherwise bring a claim without such funding. Ensuring access to justice is seen as an appropriate, even if competing, public policy concern that justifies sanction of such agreements by the courts. As matters currently stand, it is unlikely that a Cayman court would sanction a pure contingency fee agreement between a claimant and a Cayman Islands attorney (i.e.,

the attorney is paid a percentage of the damages award) because the view may be taken that the financial incentives created could corrupt the tenor of the advice that was being provided.

Proposals for legislative reforms commenced in 2015 with a discussion paper prepared by the Law Reform Commission but have not as yet advanced towards a bill.

The Grand Court's (as yet unreported) decision in A Company v A Funder, released in late 2017, marked a watershed for the jurisdiction. The plaintiff, a well-resourced business, had obtained third party funding in order to manage the risk and costs of enforcing an arbitral award against the proceeds of a fraud dispersed across the world. The search for assets led the plaintiff to the Cayman Islands. The plaintiff, represented by Harneys, successfully sought relief from the Grand Court to facilitate the use of the funding in the substantive proceedings, which would otherwise have comprised maintenance for which civil and criminal liability, at least in theory, still exists.

With the assistance of the authorities of other common law jurisdictions, the plaintiff successfully demonstrated that an appropriately formulated funding agreement would not corrupt public justice or endanger the integrity of the litigation process (being the objectives that, once upon a time, the torts sought to achieve) in a modern day legal system.

The Grand Court's decision brings the Cayman Islands into line with international onshore jurisdictions and also specifically acknowledges the global trend that third party funding is sought, not only by impecunious claimants, but also by well-resourced ones who are looking to manage the costs and risks associated with litigation.

Why the Cayman Islands?

Cayman is a popular (and increasingly so) global and investment financial center, a hub for investment funds, structured finance and private equity transactions, and trusts. There are a thousand or so Cayman incorporated companies listed on the Hong Kong stock exchange (around half of the total listed) and hundreds more on other major stock exchanges, including the NYSE, NASDAQ and Singapore.

High profile and high value disputes inevitably follow financial activity of this scale. The Cayman courts have regularly served as a venue for litigation that has captured the world's attention, most recently the year-long hearing of Ahmad Hamad Algosaibi & Brothers Company v Al-Sanea & Ors, a multi-billion dollar claim involving allegations of fraud arising from one of the largest corporate collapses of the global financial crisis. The Cayman courts also host a range of fund and trust disputes, shareholder disputes, and is a hub for cross border insolvencies and restructurings.

Financial litigation of this nature, which is unique to the off-shore world, is an attractive opportunity to the third party funding industry. Coupled with Cayman's familiar common law system, administered by an a world class judiciary and well serviced by a deep pool of legal practitioners, and ultimate recourse to the Privy Council, the Cayman Islands provides stability and predictability.

Regulation - finding the balance

The Grand Court's decision in A Company v A Funder coincided with an on-going discussion among the legal community that commenced when the Law Reform Commission published a discussion paper on potential avenues for reform in the area of alternative litigation funding in December 2015.

The most recent iteration of the LRC's draft bill and regulations propose that civil and criminal liability for champerty and maintenance would be abolished. This would render an application to court for approval of the arrangement unnecessary, albeit the court would retain its general supervisory jurisdiction over the litigation itself. The extent of the regulation currently proposed in the LRC's draft bill is minimal: the funding agreement must be in writing, and the return to the funder may be calculated either by reference to the quantum of funding provided or the recoveries in the litigation. This follows the example of Australia, where minimal regulation of litigation funders has facilitated the growth of a competitive and sophisticated funding industry, and England, where the industry is essentially self-regulated.

Appropriate legislative intervention and regulation is crucial to ensuring, not only that Cayman can take advantage of the opportunity that litigation funding presents, but also that it remains competitive as against other jurisdictions. Cayman incorporated companies, listed on foreign stock exchanges and conducting activity in foreign jurisdictions often have a choice of several venues for litigating their disputes. Facilitating access to third party funding will make Cayman an even more appealing choice.

Nick Hoffman
Partner
Harneys, Cayman Islands
T: +1 (345) 815 2916 E: Nick.Hoffman@harneys.com W: harneys.com

Lachlan Greig
Associate
Harneys, Cayman Islands
T: +1 (345) 815 2978 E: Lachlan.Greig@harneys.com W: harneys.com