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FINANCING CONSTRUCTION DISPUTES – AN EMEA PERSPECTIVE

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ABSTRACT

The construction industry is renowned for being one of the most cost-intensive industries around the world. A common mechanism in construction contracts is back-ended payments, i.e., the contractor undertakes the costs of construction upfront, and receives payments for the same upon achieving certain pre-defined milestones.

Complex, multifaceted construction projects have a tendency to end up in dispute, owing to a variety of reasons including delays, variations, and defective works. By the time these disputes arise, the contractor may already be low on cash flows, since it has deployed a considerable amount of resources towards completion of the project.

Such disputes create financial challenges for parties, requiring resources for legal fees, expert opinions, and other associated costs. The high costs associated with resolving these disputes often create barriers to accessing justice, particularly for smaller entities or individuals with limited financial resources. This paper attempts to explore the financing of construction disputes from the perspective of the Europe, Middle East, and Africa market – particularly focusing on litigation funding and alternative fee arrangements. It also evaluates the benefits, challenges, and future trends of financing construction disputes in the EMEA region.

The field of litigation finance has swiftly gained traction in the EMEA region in the past decade. Third-party funders provide capital to parties in exchange for a percentage of the recovery, based on a success fee model. This mechanism enables parties to pursue their claims without the underlying burden of upfront costs, thus levelling the playing field and enhancing access to justice.

The financing of construction disputes come with various benefits. It allows parties to mitigate financial risks, overcome budget constraints, and pursue meritorious claims. Financing options enable parties to engage experienced legal representation, access expert witnesses, and gather compelling evidence to strengthen their cases. By removing financial barriers, financing helps expedite resolution of disputes leading to negotiated settlements, saving time, money, and resources.

However, challenges exist in implementing financing solutions for construction disputes in the EMEA region. Ethical considerations, such as maintaining client confidentiality and avoiding conflicts of interest, ought to be carefully addressed. Regulatory frameworks and legal environments vary across jurisdictions, thereby requiring a comprehensive understanding of local laws and practices. In addition, the availability and acceptance of financing options may vary, and parties must carefully assess the terms, costs, and potential impact on their cases.

In addition to litigation finance, another emerging financing option is alternative fee arrangements. These arrangements, such as conditional fee agreements, hybrid fee structures, and capped fees, provide flexibility in billing methods and align the interests of parties and their legal counsel. Alternative fee arrangements enable in incentivizing efficiency, cost control, and early resolution of construction disputes.

Looking ahead, the future of financing construction disputes in the EMEA region appears promising. As parties become more aware of the available financing options, the demand for innovative and tailored solutions is bound to increase. Regulatory frameworks are constantly evolving to accommodate the growing market and address concerns such as confidentiality and conflict of interest. The use of technology, such as online platforms for litigation funding may further assist to streamline the financing process and enhance transparency.

In conclusion, financing construction disputes in the EMEA region presents opportunities and challenges. The availability of litigation funding and alternative fee arrangements offers potential solutions for addressing the financial complexities of construction disputes leading to the enhancement of access to justice and timely facilitation, resolution and mitigation of financial risks in construction disputes across the EMEA region.

Keywords: Litigation Finance, Construction Disputes, Access to Justice, Meritorious Claims, Ethical Considerations

1. INTRODUCTION

The construction industry is renowned for being one of the most cost-intensive industries around the world. A common mechanism in construction contracts is back-ended payments, *i.e.*, the contractor undertakes the cost of construction upfront, and receives payments for the same upon achieving certain pre-defined milestones.

The Europe, Middle East and Africa ("**EMEA**") region, like any other region, undertakes a diverse set of construction activities such as:

(a) Residential construction: These include residential buildings, apartment complexes, and housing developments.

(b) Commercial construction: These include commercial buildings including office spaces, retail stores, F&B chains, entertainment venues, and mixed-use developments.

(c) Industrial construction: These include factories, warehouses, and manufacturing facilities.

(d) Infrastructure projects: These include roads, highways, bridges, airports, railways, and public transportation systems.

(e) Energy and utilities projects: These include power plants, renewable energy facilities, and transmission lines.

(f) Hospitality and tourism projects: These include hotel construction, resorts, and spas.

(g) Sports and entertainment facilities: These include stadiums, arenas, sports complexes, and entertainment venues.

Time and again, it has been seen that such complex and multi-faceted construction projects have a tendency to end up in a dispute, owing to a variety of reasons. Typically, construction projects face the following kinds of disputes:

(a) Payment issues: These include non-payment or delayed payment of invoices, disputes payment amounts, and issues with payment certification.

(b) Variations or change orders: These arise from changes in the scope of work or design furnished by the employer, leading to the expenditure of additional time and costs by the contractor.

(c) Delay claims: These are caused by a host of factors including variations to the contractor's scope of work, labour or resource shortages, inclement weather, and supply chain disruptions, which lead to the contractor seeking an extension of time to complete the works.

(d) Quality and defects issues: These are related to the quality of the work and proper functioning, generally raised by the employer at the time of certification of the work.

(e) Design issues: These arise from potential discrepancies or errors in project plans, specifications, or design documents.

Due to the back-ended payment mechanism, by the time these disputes arise, the contractor may already be low on cash flows, since it has deployed a considerable amount of resources towards completion of the project.

Construction disputes such as these, complex in their very nature, as they are, have increasingly led to creation of financial hurdles for parties, inter alia requiring resources not only for completing the project, but also for legal fees, expert opinions, and other associated costs. The high costs associated with resolution of complex construction disputes often create barriers to accessing justice, particularly for smaller entities or individuals with limited financial resources.

With regard to tackling challenges associated with increasing costs associated with litigations, the field of third-party funding arrangements or litigation finance (as it is commonly known) has swiftly gained traction, particularly in the EMEA region.

Litigation financiers or third-party funders operate in a very unique manner. They are unrelated third parties providing non-recourse finance to a party in a litigation in exchange for a percentage of the recovery, based on a success fee model. This mechanism enables parties to pursue their claims without the underlying burden of upfront costs, which invariably come with litigation, thus levelling the playing field and enhancing access to justice.

Third-party funding, often referred to as litigation finance, is a mechanism by which a non-party to litigation provides funding to a party, typically in exchange for a share of the proceeds from the claim. This allows parties, especially those with limited financial resources, to pursue or defend a claim without bearing the financial risks themselves.

The EMEA region has seen significant developments in third-party funding over the past years.

(a) Europe:

   (i) United Kingdom: The UK is one of the most mature markets for third-party funding. Litigation funding is particularly popular in London, which is a global hub for commercial litigation and arbitration. The Association of Litigation Funders ("**ALF**") provides self-regulation for its members, ensuring that they comply with a code of conduct.

   (ii) Germany: The market for litigation financing is growing. There are no specific regulations governing third-party funding, but the general principles of German contract law apply.

   (iii) France: While the French legal system traditionally frowned upon third-party funding, the practice has become more accepted, especially in international arbitration.

   (iv) Spain: The market is still nascent but developing, especially in the context of arbitration.

   (v) Others: Many other European countries, from the Nordics to Southern and Eastern Europe, have seen increasing interest and acceptance of third-party funding, though regulations and market maturity vary.

(b) Middle East:

   (i) United Arab Emirates (UAE): The UAE, particularly Dubai, has shown openness to third-party funding, especially in the Dubai International Financial Centre ("**DIFC**") and the Abu Dhabi Global Market ("**ADGM**"). Both jurisdictions have issued specific guidelines on third-party funding for arbitration.

   (ii) Kingdom of Saudi Arabia: Considering an increase in sovereign investments into the kingdom, the Saudi Center for Commercia Arbitration ("**SCCA**") has significantly overhauled their rules to *inter alia* include third-party funding.

   (iii) Others: Generally, the acceptance and prevalence of third-party funding vary across the Middle East, with some jurisdictions more receptive than others.

(c) Africa

   (i) South Africa: It is one of the most developed markets for third-party funding in Africa. While there is no specific legislation regulating litigation funding, it is generally permissible as long as certain conditions are met.

(ii) Mauritius: As an emerging hub for international arbitration, Mauritius has taken steps to clarify and permit third-party funding in its arbitration proceedings.

(iii) Others: The concept of third-party funding is still relatively new in many African countries. However, as the continent sees more significant commercial and investment disputes, interest in third-party funding is expected to grow.

In 2021, the global litigation funding investment market was estimated at US$ 12.2 billion and is projected to reach approximately US$ 25.8 billion by 2030 with the compound annual growth rate (**CAGR**) of roughly 9% between 2022 and 2030.[1] These numbers are increasingly being matched based purely on the number of litigation funding arrangements being entered into across the globe with the EMEA region picking up a large share of the pie, specifically in construction disputes, which statistically have remained expensive and burdensome on parties.

2. CONSTRUCTION INDUSTRY – A REGIONAL HEAVYWEIGHT

The construction industry has been a major contributor to the economy for countries in the EMEA region. Particularly, the economic performance of the GCC countries is closely linked to the performance of the construction industry.

In recent years, however, the GCC projects market has been significantly impacted due to the Covid-19 pandemic. From US$ 106 billion in 2019, the sum of contract awards in 2020 reduced drastically to US$ 71 billion. However, there has been a rebound in 2021, with the sum reaching almost US$ 116 billion.[2]

Nonetheless, the construction industry remains a key sector for the GCC countries. The Kingdom of Saudi Arabia had almost US$ 54 billion worth of contract awards, making its projects market larger than those in five other GCC countries combined.[3]

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[1] Global Litigation Funding Investment Market 2023-2032 https://www.custommarketinsights.com/report/litigation-funding-investment-market/

[2] *Deloitte GCC Powers of Construction 2023.* (n.d.). Deloitte. https://www2.deloitte.com/xe/en/pages/real-estate/articles/gcc-powers-of-construction-2023.html

[3] *Deloitte GCC Powers of Construction 2023.* (n.d.). Deloitte. https://www2.deloitte.com/xe/en/pages/real-estate/articles/gcc-powers-of-construction-2023.html

Other countries such as Qatar also have long-term plans in place for development. The Qatar National Vision 2023 has aims at transforming Qatar into an advanced country by 2030, capable of sustaining its own development and providing for a high standard of living for all of its people for generations to come. Qatar aims to achieve this through:

(a) human development;

(b) social development;

(c) economic development; and

(d) environmental development.[4]

Qatar's construction market is set to grow at a CAGR of 9.5% from 2023 to 2030, and is projected to reach US$ 123 billion.[5] It has been reported that in the 2021 budget, the Qatar government identified new projects valued at US$ 14.8 billion, to be awarded between 2021 and 2023.[6]

Similarly, the UAE is another region where the construction industry is a key driving factor for the economy. This includes major investment in the construction of commercial and luxury properties, and development of roadways.

For instance, as a part of its 10-year future development plan, the Emirates has announced an investment of US$ 1.36 billion for the development of roadways.[7] Moreover, the construction industry in the UAE is expected to grow by 6.9% to reach AED 265,969 million in 2023.[8]

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[4] Government Communications Office. (2023). *Qatar National Vision 2030*. Government Communications Office. https://www.gco.gov.qa/en/about-qatar/national-vision2030/

[5] Maceda, C. (2023, January 10). Qatar construction market to more than double to $123.1bln by 2030. ACE Times. https://www.zawya.com/en/business/real-estate/qatar-construction-market-to-more-than-double-to-1231bln-by-2030-bpc890cv

[6] *Ibid*

[7] UAE Unveils $1.36bn Plan To Reduce Dubai Traffic Congestion. Transport Advancement. https://www.transportadvancement.com/road-traffic/uae-unveils-1-36bn-plan-to-reduce-dubai-traffic-congestion/

[8] United Arab Emirates Construction Industry Databook 2023. https://finance.yahoo.com/news/united-arab-emirates-construction-industry-115300041.html#:~:text=Construction%20industry%20in%20United%20Arab,construction%20industry%20at%20country%20level.

3. GENESIS OF LITIGATION FINANCE IN THE EMEA REGION

Litigation funding has been riding the crest of the litigation wave for some years. In many cases, it has been a happy marriage between providing access to justice and gaining profits from the proceeds.[9] Litigation funding has specifically blossomed in the EMEA region as the next big thing, increasingly turning heads everywhere.

At first glance, one might think that litigation financing is a tool primarily directed towards impecunious parties that would otherwise not be able to afford the costs associated with a complex dispute. However, litigation financing has not only become a viable tool for financially stable entities but is also being increasingly looked at as an alternative model for such entities to facilitate smooth cashflow management.

A number of globally recognized arbitral institutions have addressed third party funding in their institutional rules, which has ushered in a new era of litigation support provided by these institutions.

The very first institutional rules which addressed third party funding were the Singapore International Arbitration Centre ("**SIAC**")[10] and China International Economic and Trade arbitration commission ("**CIETAC**") investment arbitration rules[11] back in 2017, followed by the Hong Kong International Arbitration Centre ("**HKIAC**") arbitration rules[12] in 2018, the Beijing Arbitration Commission ("**BAC**") investment arbitration rules[13] in 2019, the Milan Chamber of Arbitration ("**CAM**") rules[14] in 2020 (which have further been synthesized in February 2023 and

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[9] Greene, D. (2023, April 28). Litigation funding: is the party over? https://www.newlawjournal.co.uk/docs/default-source/article_files/nlj_2023_28_apr_comment_greenedb657db6-7e5b-4f90-9fc9-be16efb71a99.pdf?sfvrsn=4d0bd7f4_1

[10] Article 24(l) of the SIAC Investment arbitration rules https://siac.org.sg/siac-investment-rules-2017

[11] Article 27 of the CIETAC International Investment arbitration rules https://droitfrancechine.org/wp-content/uploads/2019/01/CIETAC-International-Investment-Arbitration-Rules-China-International-Economic-and-Trade-Arbitration-Commission.html#:~:text=In%20these%20Rules%2C%20a%20%E2%80%9Cthird,2.

[12] Article 44 of the HKIAC arbitration rules https://www.hkiac.org/arbitration/rules-practice-notes/hkiac-administered-2018

[13] Article 39 of the BAC Investment arbitration rules https://www.bjac.org.cn/page/data_dl/touzi_en.pdf

[14] Article 43 of the CAM arbitration rules https://www.camera-arbitrale.it/upload/documenti/arbitrato/cam%20arbitration%20rules%202020.pdf

continue to include third party funding within its fold), the International Chamber of Commerce ("**ICC**") arbitration rules[15] and the Vienna International Arbitral Centre ("**VIAC**") investment arbitration rules[16] in 2021.

Importantly, the Member States of the International Centre for Settlement of Investment Disputes ("**ICSID**") have approved a comprehensive reform of its rules and regulations, including the introduction of new rules of procedure, drafted over a five-year consultation process, with a profound amendment aiming to *"modernize, simplify and streamline the rules"*. This new dawn of modernization has heralded the introduction of third-party funding[17] within the fold of investor-state disputes.

Third party funding provisions have also been considered to overhaul the DNA of international arbitration[18] and can also be found in some 'new-generation' treaties with investment provisions. For instance, third party funding is addressed in various ways in:

(a) the EU-Canada Comprehensive Economic and Trade Agreement;

(b) the EU-Singapore Investment Protection Agreement;

(c) the Canada-Chile Free Trade Agreement;

(d) the 2021 Canada Model Bilateral Investment Treaty ("**BIT**"); and

(e) the 2019 Netherlands Model BIT.

These apart, third-party funding has also been addressed within the context of negotiations on the 'modernization' of the Energy Charter Treaty.[19]

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[15] Article 11(7) of the ICC arbitration rules https://iccwbo.org/dispute-resolution/dispute-resolution-services/arbitration/rules-procedure/2021-arbitration-rules/

[16] Article 13(a) of the VIAC investment arbitration rules https://www.viac.eu/en/investment-arbitration/content/vienna-rules-investment-2021-online

[17] Favro, A. (2022, June 3). New ICSID Arbitration Rules: A Further Step in The Regulation of Third-Party Funding. https://arbitrationblog.kluwerarbitration.com/2022/06/03/new-icsid-arbitration-rules-a-further-step-in-the-regulation-of-third-party-funding/

[18] Haeri, H. (n.d.). Third-Party Funding in International Arbitration. Global Arbitration Review. https://globalarbitrationreview.com/guide/the-guide-ma-arbitration/4th-edition/article/third-party-funding-in-international-arbitration#footnote-049

[19] Modernisation of the ECT. https://www.energychartertreaty.org/modernisation-of-the-treaty/

Third party funding has also been a subject of much discussion and is being considered by the UNCITRAL Working Group III[20] within the scope of its work on investor-state dispute settlement reform. In particular, during the working group's deliberations, concerns have been identified regarding the effects of third-party funding on arbitral proceedings and on the investor-state dispute settlement system. The UNCITRAL Secretariat recognized that third party funding remain largely unregulated and suggested a range of reform options.

Specifically, this rise of a new type of party although not entirely 'vested' has provoked various concerns, mainly related to possible conflicts of interests that may arise out of relationships between litigation funders and arbitrators, counsels or parties.

While parts of the European Union, specifically the United Kingdom, pre-Brexit and even now, remain increasingly active towards litigation financing arrangements taking bulk of the global share, these have seen a seesaw effect in the larger region, particularly in part stemming from changing political landscapes and ideologies arising out of major developments which have taken place in the last half decade in the EMEA region.

In Europe, those seeking regulatory control on litigation funding have been, to some extent, successful in persuading policymakers of the need to control the funding process and consequently the market, which represents a conservative but yet still a developing or to put it simply an easing of the market towards litigation funding as an effective tool in litigation.[21]

The European Parliament has proposed to adopt a far stricter regime in the European Union (**EU**) in their resolution dated 13 September 2022 ("**European Resolution**"),[22] envisaging a draft directive on the regulation of third-party litigation funding ("**Draft Directive**"), *inter alia*:

(a) create an authorization system for funders intending to operate in the EU, including capital

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[20] UNCITRAL Third Party Funding. https://uncitral.un.org/en/thirdpartyfunding

[21] Greene, D. (2023, April 28). Litigation funding: is the party over? https://www.newlawjournal.co.uk/docs/default-source/article_files/nlj_2023_28_apr_comment_greenedb657db6-7e5b-4f90-9fc9-be16efb71a99.pdf?sfvrsn=4d0bd7f4_1

[22] European Parliament resolution of 13 September 2022 with recommendations to the Commission on Responsible private funding of litigation (2020/2130(INL))

adequacy requirements and the set-up of dedicated supervisory authorities;[23]

(b) introduce a fiduciary duty for the funders *vis-à-vis* their clients;[24]

(c) set up minimum mandatory requirements for the funding agreements;[25]

(d) prohibit influencing the management of the dispute;[26]

(e) set a cap on the funder's profit at 40 percent of the award;[27]

(f) prohibit funders from contractually limiting their liability regarding adverse costs;[28] and

(g) create an obligation to disclose *inter alia* a *"complete and unredacted copy"* of the funding agreement upon request of the court/tribunal or the opposing party.[29]

It is now upon the European Commission to submit the text of the Draft Directive to the European Parliament and the EU Council for their vote. If the Draft Directive is eventually approved and enters into force, the EU Member States will be bound to align the respective legal systems to the above-mentioned principles, thereby creating a uniform regulatory framework that might deeply affect the future of third-party funding in Europe.[30]

The International Legal Finance Association ("**ILFA**") criticized the European Parliament's proposed rules for undermining the availability of legal finance in the EU and denying access to justice.[31] The ILFA's main criticisms centered around a claimed lack of evidence or consultation

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[23] Article 4 and 6 of the Draft Directive

[24] Article 7 of the Draft Directive

[25] Article 12 of the Draft Directive

[26] Article 14(2) of the draft Directive

[27] Article 14(3) of the Draft Directive

[28] Article 14(5) of the Draft Directive

[29] Article 16(1) of the Draft Directive

[30] Favro, A. (2022, June 3). New ICSID Arbitration Rules: A Further Step in The Regulation of Third-Party Funding. https://arbitrationblog.kluwerarbitration.com/2022/06/03/new-icsid-arbitration-rules-a-further-step-in-the-regulation-of-third-party-funding/

[31] International Legal Finance Association: Resourcing the Rule of Law in Europe – June 2023

with relevant stakeholders underlying the Voss report,[32] which the proposed regulation was based on. ILFA also called for delaying introducing any major changes to litigation funding until the Draft Directive is fully transposed in all member states and has begun to bed in.[33]

Multiple developments on a global level have heralded a transition and evolution with third party funding being looked at closely by arbitral institutions in the Middle East region, specifically.

The regional powerhouse of the middle east, *viz.,* Dubai, through the Dubai International Arbitration Centre ("**DIAC**") arbitration rules, has created a paradigm shift[34] for becoming a global arbitration hub, through a genuine overhaul and modernization of the arbitration landscape in the Middle East. This has importantly introduced third party funding[35] resulting in a trickle effect in the region.

Meanwhile, the ADGM arbitration rules have also unveiled an innovative update to their rules with third party funding as their centerpiece amendment.[36]

Following suit, the much talked about SCCA rules in their second edition, have comprehensively overhauled the landscape in line with international best practices with the inclusion of third-party funding reflecting the growing prevalence of the phenomenon in the region.[37]

Changes have also been made with amendments to laws, introduction of rules and practice

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[32] Draft Report with recommendations to the Commission on Responsible private funding of litigation (2020/2130(INL)). https://www.europarl.europa.eu/doceo/document/A-9-2022-0218_EN.html

[33] Jones, E. (2023, July 7). EU third-party litigation funding regulation delayed until further studies. Pinsent Masons. https://www.pinsentmasons.com/out-law/news/eu-third-party-litigation-funding-regulation-delayed-until-further-studies

[34] DIAC Arbitration Rules 2022 – a paradigm shift for Dubai becoming a global arbitration hub. (n.d.). https://www.ibanet.org/diac-arbitration-rules-2022-dubai

[35] Capital, E. (2022, October 12). Renewal Of DIAC Rules Include Updates On Third Party Funding And Costs Recovery. Arbitration & Dispute Resolution - United States. https://www.mondaq.com/unitedstates/arbitration-dispute-resolution/1203696/renewal-of-diac-rules-include-updates-on-third-party-funding-and-costs-recovery

[36] Blanke, G. (2021, March 3). Amendment No. 1 of 2020: The 2015 ADGM Arbitration Regulations in Focus. https://arbitrationblog.kluwerarbitration.com/2021/03/03/amendment-no-1-of-2020-the-2015-adgm-arbitration-regulations-in-focus/

[37] SCCA Arbitration Rules 2023 – a further step in the right direction? — Financier Worldwide. (n.d.). Financier Worldwide. https://www.financierworldwide.com/scca-arbitration-rules-2023-a-further-step-in-the-right-direction

directions to give effect to third party funding, and arrangements which are increasingly becoming the go-to requirement for the mecca of construction disputes. The DIFC[38] and ADGM[39] have both introduced third party funding within their legal framework, representing a change in the tide for dispute resolution in the Middle East.

It is not short to mention that historically the DIFC courts[40] have recognized the existence of third-party funding agreements, which paved way for the introduction of the aforementioned practice directions and amendments.

Thus, over time the idea of third-party funding has transgressed from a European centric concept to the larger EMEA region with an increased confidence amongst parties across the region to approach litigation funders who are considered an important cog in the dispute wheel, specifically construction sector which share the bulk of disputes in the region.

4. EMERGENCE OF LITIGATION FINANCE

Third-party funding or litigation finance has gained traction as it has become a significant support mechanism for construction companies, particularly during these challenging economic times, considering it enables businesses to maintain operations, pursue growth opportunities, and navigate period of economic uncertainty.

Some of the key attributes and factors which have ensured that litigation finance is a necessary enabler and has gained traction in the EMEA region, particularly in the construction sector thereby allowing companies to remain afloat are:

(a) Liquidity Boost: One of the primary benefits of third-party funding is that it provides immediate liquidity. For companies facing cash-flow problems or unforeseen expenses,

[38] DIFC Courts Practice Direction No. 2 of 2017 on Third Party Funding. https://www.difccourts.ae/rules-decisions/practice-directions/practice-direction-no-2-of-2017-on-third-party-funding-in-the-difc-courts

[39] ADGM Courts, Civil Evidence, Judgments, Enforcement and Judicial Appointments Regulations 2015. https://en.adgm.thomsonreuters.com/sites/default/files/net_file_store/ADGM_Courts_Regulations_2015_Amended_18_December_2018.pdf; Litigation Funding Rules 2019. https://www.adgm.com/documents/courts/legislation-and-procedures/legislation/rules/litigation-funding-rules-2019.pdf

[40] Rafed Al Khorafi and Others v Bank Sarasin-Alpen (ME) Ltd and Bank Sarasin & Co Ltd *(DIFC Courts – 21 August 2014 - CFI 026/2009)* and Vannin Capital Pcc Plc v Mr Rafed Abdel Mohsen Bader Al Khorafi and others *(DIFC Courts – 18 April 2016 - CFI 036/2014)*

external funding can offer a lifeline, specifically in disputes.

(b) Risk Sharing: Third-party financing, especially in litigation finance, can share the risk of costly legal battles. Companies can pursue legitimate claims without bearing the full financial burden themselves.

(c) Flexibility: Different third-party financiers offer varied terms, giving companies the flexibility to choose a structure that best fits their needs.

(d) Expanding Growth Opportunities: External financing can help companies invest in new projects, research and development, or expand into new markets. Even during tough times, this can allow a company to grow, innovate, and potentially capture larger market shares, while being comfortable that disputes are being looked after.

(e) Restructuring Debt: Companies facing high debt burdens can use third-party funding to restructure or refinance existing obligations, potentially securing better terms or lower interest rates.

(f) Buffer against Economic Downturns: During economic recessions or downturns, many companies experience decreased revenues. Third-party funding can serve as a buffer, enabling companies to continue operations, retain employees, and maintain market presence until economic conditions improve. This also improves business outlook for various companies who can look to invest more in their business as opposed to being cash strapped.

(g) Stakeholder Confidence: Securing funding often signals to stakeholders (like customers, suppliers, and even employees) that the company has the backing and confidence of financiers, potentially leading to better business relationships and morale.

(h) Expertise and Networking: Many third-party financiers offer more than just capital. They provide subject matter expertise, mentorship, and networking opportunities that can help businesses navigate challenging times.

(i) Bridging Gaps in Traditional Financing**:** There are times when traditional banks and financial institutions become risk-averse, particularly during economic downturns and when companies are faced with complex disputes. In such times, third-party financiers, can step in to fill the financing gap.

Third-party funding thus plays an essential role in modern business ecosystems, offering both financial support and strategic advantages to companies navigating challenging periods. However, like all financial tools, it is vital for businesses to understand the terms and implications of external financing and ensure it abides by long-term strategy and objectives.

While there is the element of access to justice deeply rooted in the idea of litigation funding, it ought not be considered that litigation funding is somewhat philanthropic, driven purely by the access to justice dynamic. Litigation funders are serious business makers who invariably like all business-driven minds are seeking profitable returns out of this alternative investment class. It is risky business and if the returns do not achieve a profit, taking into account the risk, the funders are unlikely to flinch and have a second look irrespective of the justice which is at stake.[41]

5. CHALLENGES AND ETHICAL CONSIDERATIONS

Historically, the doctrines of champerty and maintenance were established to prevent meddling in litigation by unrelated third parties. "Maintenance" is the support of litigation by a stranger who has no legitimate concern in the litigation, whereas "champerty" is a form of maintenance in which the stranger would receive a portion of the litigation proceeds. The rationale behind these doctrines was to prevent the wealthy from manipulating the legal system and potentially bringing frivolous or vexatious litigation.

In modern times, rigid application of these doctrines has been viewed by many jurisdictions as outdated. The landscape of litigation has shifted significantly, and the prohibitions against third-party funding have been seen as a barrier to access to justice, especially when litigants lack the resources to pursue or defend their rights. This has led to the dawn of litigation funding, which provides unique reasons why it has significantly gained traction:

(a) Access to Justice: It enables individuals or entities that might not have the financial capacity to pursue litigation to assert their rights.

(b) Risk Spreading: Litigation funding allows for the spreading of risk. This is especially relevant

[41] Greene, D. (2023, April 28). Litigation funding: is the party over? https://www.newlawjournal.co.uk/docs/default-source/article_files/nlj_2023_28_apr_comment_greenedb657db6-7e5b-4f90-9fc9-be16efb71a99.pdf?sfvrsn=4d0bd7f4_1

in high-stakes litigation.

(c) Counsel on Merits: Funders usually undertake thorough due-diligence before investing, which can serve as an additional layer of scrutiny on the merits of a case.

(d) Shift in Perception: The ethical concerns regarding third-party involvement have waned as the benefits of litigation funding have become more apparent.

Some sceptics may question the need to tightly regulate litigation funding, a question which is difficult to grapple with and present complex challenges, with compelling arguments on both sides:

(a) Advantages of Strict Regulation:

  (i) Protecting Vulnerable Litigants: It ensures that litigants are not taken advantage of by funders who might demand an excessive portion of the litigation proceeds.

  (ii) Preventing Frivolous Litigation: Regulations can ensure that only meritorious claims are pursued.

  (iii) Transparency: It ensures that all parties are aware of who is funding litigation and for what purpose.

(b) Drawbacks of Strict Regulation:

  (i) Barrier to Entry: Over-regulation might deter litigation funders from operating in certain jurisdictions, which could restrict access to justice.

  (ii) Stifling Innovation: Too much regulation might stifle innovative funding models and solutions that could be beneficial to litigants.

  (iii) <u>Increased Costs:</u> Regulatory compliance can be expensive, potentially raising the costs of litigation funding and, by extension, reducing the amounts available to litigants.

The litigation finance industry has grown in prominence having seen the establishment of several specialized associations and organizations that provide guidelines and best practices for their members. Some of these organizations include ILFA, ALF, and the European Legal Finance Association ("**ELFA**"). Each of these organizations have setup specialized rules, best practices and, or code ethics and conduct to ensure ethical, transparent and professional dealings amongst members.

ALF's code of conduct[42] is focused on capital adequacy of funders, termination and approval of settlements and control amongst other important areas. Similarly, ILFA members have each committed to uphold best practices[43] which are avoidance of conflict of interest, clarity, respecting duties to the court, preservation of confidentiality and legal privilege, etc. The ELFA also has set a largely similar code of conduct for their members[44]. These rules, code of conduct and best practices allow litigation funders to adhere to a set international benchmark of professionalism.

Litigation finance is sometimes confused with usury laws, which set a maximum lawful interest rate that can be charged on loans, which if exceed are considered usurious and could be subject to penalties. However, litigation finance is far from being a traditional loan. The principal reason for concluding that litigation finance is not lending is that litigation finance almost always involves a non-recourse payment to the litigant. That is, the litigant's duty to repay the advance is contingent, not absolute.[45]

In a nutshell, the following are the distinct reasons why litigation finance is not a loan:

(a) Non-recourse nature: Traditional loans require repayment no matter what the outcome. However, litigation funding is typically non-recourse, meaning if the party does not win or settle the case, they don't owe anything to the funder.

(b) Investment vs. Loan: Litigation funding is also more akin to an investment in the outcome of a lawsuit, rather than a loan. The funder takes on the risk of losing their investment if the case is unsuccessful.

Courts have therefore held that usury laws do not prohibit litigation finance arrangements. Usury laws apply to loans, which are distinct in their nature in their absolute requirement that a borrower

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[42] ALF Code of Conduct for Litigation Funders (2018) https://associationoflitigationfunders.com/wp-content/uploads/2018/03/Code-Of-Conduct-for-Litigation-Funders-at-Jan-2018-FINAL.pdf

[43] ILFA Best Practices https://www.ilfa.com/

[44] ELFA Code of Conduct (Adopted by the Board of Directors on 29 June 2022) https://elfassociation.eu/about/code-of-conduct#:~:text=Funders'%20commitment%20to%20maintain%20capital%20adequacy&text=Shall%20at%20all%20times%20have,articles%20of%20incorporation%20of%20ELFA.

[45] Elias. (2017, December). Mythbusting: Why the critics of litigation finance are wrong. Retrieved January 15, 2024, from https://www.fedbar.org/wp-content/uploads/2017/12/Mythbusting-pdf-1.pdf

must repay. Litigation funders to the contrary are repaid only if the party wins.[46]

Key factors while engaging with litigation funders include considerations such as privilege, control, and disclosure:

(a) Privilege:

(i) Attorney-Client Privilege: Sharing information with a third-party (like a litigation funder) can sometimes jeopardize the protection of attorney-client privileged communications. However, in many jurisdictions, if the third-party shares a common interest in the litigation, then the privilege can be maintained. It is essential to structure the litigation financing arrangement carefully to preserve this privilege.

(ii) Work Product Doctrine: This protects materials prepared in anticipation of litigation from discovery. Sharing these materials with a funder might raise concerns, but many courts have found that sharing with a litigation funder does not waive this protection.[47]

(b) Control:

(i) Decision-making Authority: One of the significant concerns is who retains control over the litigation strategy, including whether to settle and for how much. In many reputable funding agreements, the funder does not control the litigation or settlement decisions, which remain with the plaintiff and their attorney. This is a critical point to clarify in any funding agreement.

(ii) Ethical Concerns: Lawyers have an ethical duty to represent their clients zealously and without interference. Any agreement that potentially allows a third party, like a funder, to influence the attorney's professional judgment can be ethically problematic. This is why control provisions are crucial.

(c) Disclosure:

(i) Transparency with the Court: Some jurisdictions require, or at least allow for, the

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[46] Litigation Finance Investments Are Not Risk-Free Loans | Validity Finance. (2020, June 15). Validity Finance. https://www.validityfinance.com/news/thought-leadership/2020-06-15-lit-finance-not-a-loan#:~:text=And%20it%20is%20why%20courts,only%20if%20the%20plaintiff%20wins

[47] see, by way of example in the United States, *Fulton v. Foley*, 2019 WL 6609298; *Continental Circuits v. Intel Corp.*, 435 F. Supp. 3d 1014 (D. Ariz. 2020); *Miller UK v Caterpillar*, 17 F.Supp.3d 711 (Illinois)

disclosure of third-party funding arrangements. This is to ensure transparency and to address any potential conflicts of interest or ethical issues.

(ii) Transparency with the Opposing Party: Whether or not to disclose the existence of litigation financing to the opposing party is a strategic and sometimes legally-mandated decision. While it might be advantageous in some scenarios (e.g., signalling the strength of the claim), it might not be in others.

(iii) Confidentiality Agreements: When engaging with potential funders, claimholders and their lawyers often enter into confidentiality agreements to protect sensitive information.

Therefore, while litigation finance is an evolving industry and there are varied views of the courts and jurisdictions on issues pertaining to litigation finance, it is essential to be well-informed and cautious. Claimholders and lawyers must work together closely, potentially with expert consultants when navigating the intricacies surrounding litigation funding agreements, since these invariably are distinct and specific to the dynamic of a particular case.

6. CONSEQUENCES AND IMPLICATIONS OF PACCAR ON THE LITIGATION FINANCE INDUSTRY IN THE EMEA REGION

The now landmark judgment delivered by the Supreme Court of the United Kingdom in PACCAR[48] held by a 4:1 majority that litigation finance agreements ("**LFAs**") which entitle funders to payment based on the amount of damages recovered are 'damages-based agreements' ("**DBAs**"). As a result, such LFAs are unenforceable unless they comply with the regulatory regime for DBAs.

The decision concerned important matters of statutory interpretation in the context of litigation funding and issues surrounding collective proceedings brought out for breaches of competition law. Under English competition law, in order to obtain collective proceedings, a party is required to show adequate funding arrangements in place to meet their own costs as also any adverse costs order made against them should they lose. Interestingly, one of the parties relied on LFAs in an effort to meet these requirements.

In particular, PACCAR considered whether each of the agreements to provide LFAs constituted

[48] PACCAR Inc & Ors. v Competition Appeal Tribunal & Ors. [2023] UKSC 28

DBAs, a specific term statutorily defined. In order to be lawful and enforceable a DBA was required to satisfy certain conditions and these LFAs were entered into without satisfaction of these specified conditions. These were not met and in any event a DBA if it relates to opt out collective proceedings shall be unenforceable.

The litigation funders have had a good gestation period in the UK market, being operational in the industry for close to two decades. These funders have adopted methods for calculation of their return in numerous permutations and combinations, mostly favoured between taking a percentage of damages, multiple of invested capital or a combination of both.[49]

These may be worrying times for the litigation funders and for law firms that rely upon them for funding within the United Kingdom, since all LFAs will now be under the scanner to be reviewed by litigation funders, funded parties and their lawyers and under increasing scrutiny by counter-parties and the Courts and, or Tribunal and one must anticipate further challenges to commence.

Some sceptics are also of the view that while PACCAR will not be generally expected to impact the economics of legal finance and will not be successful in deterring willingness to financing of meritorious claims, it might still affect how LFAs are structured such that there is compliance to the regulatory framework.[50] Meanwhile, individual financiers will definitely still consider if any changes are the need of the hour to their own LFAs as a direct consequence of PACCAR.

Nevertheless, it is a given that PACCAR will undoubtedly have an effect on funding agreements in opt-out collective proceedings in the Competition Appeal Tribunal ("**CAT**"), particularly since most collective proceedings in the CAT are invariably reliant on litigation funding.[51]

The decision in PACCAR is considered by many a self-inflicted injury by the English courts and there will be issues and delays but by no means will it result in anarchy within the litigation finance

[49] Davies, N. (n.d.). What next for the UK litigation finance industry? https://www.linkedin.com/pulse/what-next-uk-litigation-finance-industry-nick-rowles-davies/?utm_source=share&utm_medium=member_android&utm_campaign=share_via

[50] Cross, M. (n.d.). "Shockwaves" as Supreme Court rules litigation funding deals unenforceable. Law Gazette. https://www.lawgazette.co.uk/law/shockwaves-as-supreme-court-rules-litigation-funding-deals-unenforceable/5116775.article

[51] Supreme Court litigation funding judgment threatens viability of collective claims. (n.d.). The Global Legal Post. https://www.globallegalpost.com/news/supreme-court-litigation-funding-judgment-threatens-viability-of-collective-claims-1990583922

industry.[52] An immediate effect is the likelihood that some of the litigation funders in the United Kingdom may not survive this and the immediate paralysis brought about by the distraction of satellite litigation and challenges from historic funded parties will inevitably be fatal for some. However, this does present an increasingly lucrative opportunity for litigation funders based in the EMEA region and elsewhere to capitalize on the vacuum which may be left behind. Although it may be a relatively small void to fill, it will represent a growing interest in litigation funding and an opportunity for the EMEA region to increase their activity in litigation funding which still has managed to weather shockwaves created by PACCAR.

The litigation finance industry was not and is not prepared for this turn of events considering the storm litigation finance has created in the industry over the past decade or so. This was indeed a very unhelpful judgment for funders situated in the United Kingdom and the effects it may have ought not to be underestimated.[53] However, it is safe to say that PACCAR while having widespread ramifications is distinct to the United Kingdom and English law and until it is relied on in other jurisdictions, remains a local but yet significant phenomenon.

7. FUTURE OF FINANCING CONSTRUCTION DISPUTES

Over the years, the litigation finance industry has weathered many a storm and has positioned itself for incremental growth notwithstanding an economic downturn. The road has been smooth but for certain minor speed bumps in the journey and the practice will continue to grow among law firms, corporations and industry professionals alike as they become accustomed to this effective tool called litigation finance.

An interesting characteristic of the litigation finance industry is that it is uncorrelated to the market and while the economy may have witnessed a downturn, the litigation finance industry is witnessing an uptick in growth as litigation funders are expecting to raise more capital if a downturn or recession occurs in the coming years.[54]

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[52] UK Supreme Court deals blow to litigation funding industry. (n.d.). Financial Times. https://www.ft.com/content/7ed8e9c4-e733-4601-8499-1c6aab278515

[53] Davies, N. (n.d.). What next for the UK litigation finance industry? https://www.linkedin.com/pulse/what-next-uk-litigation-finance-industry-nick-rowles-davies/?utm_source=share&utm_medium=member_android&utm_campaign=share_via

[54] Pavia, A. (2022, November 14). ANALYSIS: Are Boom Times Ahead for Litigation Finance? https://news.bloomberglaw.com/bloomberg-law-analysis/analysis-are-boom-times-ahead-for-litigation-finance

The Russia-Ukraine conflict is a fraction point of discussion amongst industry leaders since it has now become certain that it may cause an exponential spurt in construction industry claims in the EMEA region owing to rising costs, thereby leading to litigation funders becoming increasingly busy and curating innovative approaches around financing such claims. Ukraine is also likely to fund the bulk of their post-war recovery from the resources of western powers having confiscated assets of Russian oligarchs across the Americas and EMEA region.[55] This is consistent with the European commission unveiling a platform for international banks and institutions to oversee and help assist in reconstruction of Ukraine's economy post the war.

On the other side of the Middle East, the FIFA World Cup, although a resounding success, was marred with a spate of controversies from human rights violations to construction and project claims by contractors which has led to an increase in construction disputes in the region. As the work for contractors in Qatar winds down, many are retrenching. There is also a level of scepticism around bad debts and the extent to which these will filter through to full blown restructuring in a market which has been historically averse, with litigation funders on the look-out for attractive investment options.[56]

The European Commission has also taken a leadership role in addressing climate change, which has led to EU Courts in escalating a major multijurisdictional case holding governments accountable for missing climate goals leading to parties seeking new ways to recoup their losses and parties are weighing up options and benefits in settling climate disputes, with litigation finance an attractive avenue.[57] This has been exasperated with the environmental commitments made at COP26 and potential situations arising out of COP28 leading to climate driven disasters which have an impact on failing infrastructure arising out of potential defects which will lead to a further

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[55] Smith-Meyer, B., & Wheaton, S. (2022, July 6). Funding Ukraine's recovery with Russian riches causes legal headache. POLITICO. https://www.politico.eu/article/funding-ukraines-recovery-with-russian-riches-raises-legal-headache/

[56] Qatar set to be restructuring hotspot in 2023 in aftermath of World Cup – MENAT Weekly Comment (2023, January 23). ION Analytics Community. https://community.ionanalytics.com/qatar-set-to-be-restructuring-hotspot-in-2023-in-aftermath-of-world-cup-menat-weekly-comment

[57] What's Happening in Europe, LatAm and the Middle East Legal Markets? | Law.com International. (2022, September 29). Law.com International. https://www.law.com/international-edition/2022/09/20/whats-happening-in-europe-latam-and-the-middle-east/?slreturn=20230715042353

rise in unforeseen construction disputes in the EMEA region. Litigation funders will be quick to adapt and seek out innovative methods of raising capital and will look to achieve a profit in this new segment of construction disputes.

While third party funders have long been a resource to contractors involved in common law disputes in the regional European hub *i.e.*, United Kingdom, it is extremely interesting to witness the sea change in how funding is developing and consistently being used by contractors across the Middle East and African regions, in what appears to be just the tip of the iceberg. These reasons are exasperated due to an increase in construction disputes with the construction industry well suited to third party funding and the growing knowledge amongst corporations and industry experts as to how third-party funding can be used as an effective tool and a profitable financial solution amidst a dispute.[58]

The awareness and interest in third-party funding continues to rise and the sheer number of high value construction disputes has led the industry to look at alternative means of addressing their legal spend on disputes. The construction and energy sectors are also poised to benefit from the new and developing corporate portfolio approach to third-party funding.

Additionally, the use of the insurance market for disputes is a recent trend. One of the most common policies that parties avail of is the standard single risk adverse cost policy or ATE (after the event) insurance. As the name suggests, under this policy, the insurer takes on the adverse costs which an unsuccessful party may be ordered to pay to a successful party. Some third-party funders also offer “a package deal”, as per which the funder not only finances the costs of pursuing the dispute, but also provides insurance policies that protect against potential adverse costs.[59]

It is also not uncommon for parties to furnish such ATE insurance policies as security in situations where a party is ordered to provide security for the opposing party’s costs.

Recently, the range of products in the insurance market has started to diversify. The current insurance market is unrecognisable, as compared to what it was around 5-6 years ago. There are several new, creative policies that insurers offer. For instance, insurers provide “add-ons” to

[58] The emergence of third party funding | Driver Group Plc. (n.d.). Driver Group Plc. https://www.driver-group.com/en/europe/news/third-party-funding
[59] Arnott, C. (n.d.). Protect against adverse costs with ATE insurance | Burford Capital. Burford Capital. https://www.burfordcapital.com/insights/insights-container/adverse-costs-and-ate-insurance/

existing policies. These may include a cover for costs of disbursements or for a proportion of costs incurred by the legal representatives, as an add-on to existing ATE insurance policies. Insurers, however, are often less involved in the dispute than third-party funders. This is natural, since insurers do not stand to gain any uplift on a successful award or judgment.

Another product that has recently been introduced in the market is judgment preservation insurance. With any successful judgment, there is a risk that an appellate court may reverse or reduce the quantum of damages awarded. Judgment preservation insurance protects a successful party from this risk.

Some insurers also provide insurance-backed judgment monetization solutions, which enable successful parties to receive judgment proceeds within days after a judgment preservation insurance policy is bound, and then use those proceeds however they see fit, despite the fact that appellate proceedings or other challenges to the judgment may not resolve for many months or years.[60]

Political risk insurance is yet another new product that is being tested in the market. Under this policy, insurers may provide coverage to investors for claims against Sovereign States. If the investor is successful, and the State refuses to comply with any award of damages it may be considered as political risk, which the investor will be protected against.

8. CONCLUSION

In conclusion, third-party litigation funders and insurers have been the talk of the legal industry with all boardrooms and legal circles increasingly looking at litigation finance as an attractive yet nascent avenue and market to commit to.[61] While the coming years are sure to be interesting and important from the perspective of a litigation funder, funded parties and industry experts, the litigation financing industry is sure to no doubt witness an exponential change and increasing interest from the construction sector, regulators and politicians alike in the EMEA region.

[60] Judgment Preservation Insurance. (n.d.). https://www.aon.com/getmedia/bd8aa935-d0ae-48c7-b00a-0cd46227d82c/Aon-s-Judgment-Preservation-Insurance-Solution-Feb-2022.pdf.aspx

[61] Greene, D. (2023, April 28). Litigation funding: is the party over? https://www.newlawjournal.co.uk/docs/default-source/article_files/nlj_2023_28_apr_comment_greenedb657db6-7e5b-4f90-9fc9-be16efb71a99.pdf?sfvrsn=4d0bd7f4_1

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