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Third-Party Funding: Milan Event Offered A View Ahead

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On Friday 13 January 2017, the Italian law firm Lombardi Segni e Associati hosted an ICC YAF event on Third-Party Funding (“TPF”) at its Milan office. The debate was introduced by Philippe Pinsolle (Partner, Quinn Emmanuel), key-note speaker of the event. Yasmin Mohammad (Senior Counsel, Vannin Capital), Shannon Lazzarini (Head of Group Litigation, Unicredit) and Pietro Galizzi (Retail Market Gas & Power Legal Assistance Senior Vice President, Eni) addressed the quantitative and qualitative assessment of a possible case to be funded. Steven Friel (CEO, Woodsford Litigation Funding), Georg Scherpf (Senior Associate, Luther) and Benjamin Gottlieb (Associate, Schellenberg Wittmer) addressed the most negotiated issues and clauses of a funding agreement.

The speakers and the lively crowd discussed, among the others, a number of though-provoking comments.

TPF is a direct consequence of the 2008 financial crisis. The 2008 crisis has been regarded as responsible for several financial inconveniences and social repercussions. Regardless of the reasons behind the crisis, the financial crunch has left less money for all market players, including corporations. A few further consequences can be listed in turn here: (i) difficulties to have debts paid; (ii) low returns on traditional investments on financial markets; (iii) failure of projects and transactions; (iv) increase of disputes – both litigation and arbitration proceedings – with substantial amounts of money at stake. This is rather forthright: disputes between impecunious parties have made TPF essential for them and, at the same time, the activity of hedging the risk, as it is often opted by solvent entities, has transformed TPF into a proper fruitful business for funding entities.

What is happening now is that the application of TPF is driving its own regulation and not vice-versa. TPF is an industry which is subject to changes every day. It is well-known that a number of jurisdictions have traditionally either banned or not regulated TPF. This was the case of Singapore and Hong Kong, respectively. Although one of the conventional reasons behind TPF is to guarantee access to justice also to parties that have no financial resources to litigate/arbitrate their disputes, a long-established ground not to consider TPF has been its potential characterization as an offense to the English doctrines of maintenance and champerty. Champerty and maintenance have been considered illegal for two main public policy reasons. First off, it is considered desirable to restrain excess litigation for the effectiveness and efficiency of any judicial system. Second, and most important, champerty and maintenance are supposed to bring money to an individual who was unconnected to the essence of the dispute and not personally harmed by the other party.

Nonetheless, these common-law theories appear to be out-of-date today. England, US and Australia already provide for and encourage TPF, whilst other countries are in the process of following their steps. Singapore and Hong-Kong are meaningful examples of this cultural shift. On 10 January 2017, the Singapore Parliament amended the Civil Law Act and allowed, in principle, the use of TPF in international arbitration. Hong Kong seems to be following the same path: a few months ago, crucial legislative amendments to the Hong Kong Arbitration Ordinance were proposed, in order to formally abolish the doctrine of champerty and maintenance, and allow TPF in international arbitration. For all other jurisdictions where TPF is a reality, but legislators have not provided any guidance yet, the business is driving its own regulation.

There are three issues on which the discussions will be focused in the immediate future: consolidation, eligibility and control. The funding entities usually operate as hedge funds, dealing with financial businesses with a focus on claims. They mainly operate on a portfolio basis, which is the only way to obtain returns, and aim to transform claims into a class of assets. Having said that, consolidation means that today major funds are in the process of acquiring other funds and grow in size. From the clients' perspective, this will imply a reduced number of players in the legal services funding industry; thus, clients will have less power to leverage while negotiating a funding agreement. As to the claims' eligibility to be funded, this is and will remain necessarily limited. In addition to the reasonable high expectations to be eventually successful, eligible claims need to have some value (i.e., monetary value); the final decision needs to be capable of being enforced with a certain degree of fluency; and the party seeking funding from external resources needs to be assisted by experienced and skilled counsel. The concurrent existence of all these requirements limits substantially the range of action of TPF. Lastly, as to control, the issue whether and to what extent the third-party funder is entitled to be involved in the dispute and in the strategic determinations throughout the proceedings – up to the point to get even control over it – is still debated.

In addition to the above, the ICC YAF event in Milan was gripping also because of TPF's practical features offered by the panellists, especially by the representatives of funds and counsel with experience in TPF. Through a deep and pragmatic inspection of the process leading to a funding agreement (all the main steps were taken into consideration: from the signature of a non-disclosure agreement to the due diligence analysis, and the exclusivity agreement), the speakers laid out a funding agreement template, and explored its most common negotiated clauses. Particular focus was put on success-fee clauses and their possible distinct structures.

What about Italy?

Despite the seat of the conference, interestingly, no questions have been raised on the implementation of TPF in Italy. Here the situation is peculiar. However, there is interesting room for future improvements. In our opinion, Italy presents the suitable features to fit into this business. As a matter of fact, Italy, unfortunately, suffered from the 2008 crisis fiercely and the number of disputes involving Italian undertakings boosted over the past 8-10 years. As a consequence of the crisis and the on-going economic situation, returns on traditional investments have been drastically low. Hence, in theory a great number of parties may be interested in obtaining funds in order to handle their disputes.

However, TPF is largely foreign to Italy today. There are at least two reasons for this. First, users do not seem to feel the need to resort to litigation funding. Costs of domestic litigation before national courts are still low and affordable compared to other jurisdictions where litigating parties

can foresee significant expenditures, also in light of specific stages of the proceedings, such as the discovery. By way of example, in Italy the highest filing fee (which represents the court's costs) for a first-instance civil proceeding is €3,372. Average counsel's fees for a full-fledged civil proceeding worth around €1M can be around €30,000 (according to the parameters used by judges to award attorneys' costs and fees). Second, litigation funders might find problematic to assess certain essential elements of their investment plan, such as the length of proceedings before Italian courts (from the inception to the enforcement stage, if any) that cannot always be foreseen with certainty.

Nonetheless, it is our view that, with the increasing popularity of domestic and international arbitration, the TPF business might find its way into the Italian legal system, as also solvent parties may start to seek funding to allocate the risks in major disputes. Whereas it often seems impossible to predict future trends in the Italian legal market, the vivid interest shown in the Milan event speaks volumes about the market's appetite for this business.

The views expressed in this article are those of the authors alone and should not be regarded as representative of, or binding upon, the ICC YAF and/or Lombardi Segni e Associati.

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