

Costs awards against funders of litigation

Introduction

Since 2004 there have been a number of high profile and widely reported cases whereby directors of asset-less and near insolvent limited companies bringing unsuccessful claims to trial have been personally ordered to pay the costs of the successful Defendant, even though those directors have not actually been parties to the claim.

The days of directors proceeding with litigation, fanciful or otherwise, happy in the knowledge that the company was a separate legal entity which could simply be wound up if ordered to pay the other side's costs, with no liability falling on the director, will soon be long gone.

The current position is that where a director who is not a party to the litigation could be described as the "real party" seeking his own benefit from and controlling and/or funding the litigation, then, even where he has acted in good faith, he may well be ordered to pay the successful Defendant's costs. This is perhaps unfair where the Defendant had the opportunity at the start but failed to apply for the Claimant to provide some security to pay a potential costs order.

Overview

To track recent developments in this field, we need to go back to the important Privy Council case of *Dymocks Franchise Systems (NSW) Pty Limited -v- Todd & Others* [2004] 1 WLR 2807.

The Court held that although costs orders against non-parties to the litigation were still to be regarded as exceptional, exceptional was simply to mean no more than "outside the ordinary run of cases where parties pursued or defended claims for their own benefit and at their own expense". It is not, therefore, a particularly onerous hurdle to overcome. The real question, the Court found, was whether it was just to make the order. Further, the non-party was not only to have funded the litigation but also to have substantially controlled it, or was to have benefited from it. In such circumstances, that person ran the risk of finding himself being ordered to pay the successful party's costs.

The reasoning behind *Dymocks* was sound, albeit that in that case the costs order was made not against a director but another company. The Court found that (1) without the involvement of that third party company the Defendants would not have pursued their appeals to the Court of Appeal and Privy Council; and (2) the non-party was to have benefited from the proceedings should they have proved successful.

This results in a separate post-trial forensic exercise - who stood to reap the rewards? Note, however, that a person not standing to benefit from the result of the litigation, but supporting the Claimant for other reasons, may avoid an order for costs (to the relief, no doubt, of the many backers of Neil Hamilton in his unsuccessful libel claim against Mohammed Al Fayed *Hamilton -v- Al Fayed* (No. 2) [2002] EWCA Civ 665. [2003] QB 1175).

A degree of recklessness?

In *Gemma Limited -v- Gimson & Another* [2005] EWHC 69 (TCC), the Judge held that Mr and Mrs Davies, the respective director and company secretary of the company (Mrs Davies did not escape by virtue of her not being a director), had funded the company's claim in its entirety - and stood to benefit personally should the company have succeeded at trial. In addition (my emphasis) the Judge found that Mr and Mrs Davies had withheld information from the company's solicitors that, had it been disclosed, would have led the solicitors to advise that the company's case was hopeless. Accordingly, the litigation had been pursued unreasonably and was not in the company's best interests. In those circumstances, it is not hard to see how the Judge held Mr and Mrs Davies' behaviour to be reckless and worthy of an "exceptional" costs order.

The Current Position

The most recent in this long line of "funder" cases is *Goodwood Recoveries Limited -v- Breen* [2005] EWCA Civ 414. Goodwood takes the principle on another step and could yet open up a can of worms. In this case, as in *Gemma*, the company's litigation had been controlled (not even funded - a conditional fee agreement was in place) by a third party (and not even a director by the time the matter came to trial), a Mr Slater. The company's claim failed and the Court ordered Mr Slater to pay the successful party's costs personally. On appeal, and perhaps not unreasonably in the light of both *Dymocks* and *Gemma*, Mr Slater argued that it required exceptional conduct to render a director liable for the costs. The Court was having none of it and came down hard on Mr Slater; holding that the whole of the costs of the litigation were caused by his dishonesty. So far so good. Following *Gemma*, the Court found that the litigation had been pursued unreasonably and, coupled with Mr Slater's apparent dishonesty; the Court made another "exceptional" costs order.

The Court went further though, and this is where Claimants must be very careful in the future, holding that where a non-party director could be described as the "real party" in the litigation seeking his own benefit from and controlling and/or funding the litigation, then even where he had acted in good faith he could be ordered to pay the successful party's costs. According to *Goodwood*, therefore, it may simply be irrelevant in years to come whether or not the litigation had been pursued unreasonably or the director had acted dishonestly.

Comment

Recklessness or bad faith is no pre-requisite to a director or other non-party funder being ordered to pay the costs incurred through his company bringing an unsuccessful claim. So long as that director was to have benefited from, and controlled, the litigation, he may well be ordered to pick up the tab. Suddenly, the concept of a company's limited liability seems a long way away and it is imperative that such directors are reminded of this before proceedings are issued.

When acting for a Defendant in these circumstances, it would still be advisable to consider applying for an order for security for costs against the Claimant at an early stage rather than relying on recouping costs from a director post trial. Not only might the director himself turn out to be impecunious but also you might be able to have the litigation struck out long before trial.

Contact

Simon Hobbs
Partner
Email simon.hobbs@ibblaw.co.uk
Tel 01895 207983