GUIDANCE NOTE

Recoverability of CFA uplift and ATE Insurance Premiums in Insolvency Cases

August 2014

The Supreme Court is to consider the recoverability of CFA[1] uplift and ATE[2] insurance premiums in all cases, including insolvency cases and cases having CFAs and ATE insurance policies pre-dating 1st April 2013.

Coventry and others v Lawrence and another (No 2) [2014] UKSC 46[3]

On Wednesday 23rd July 2014 the Supreme Court handed down a judgment which opens up the prospect of non-recoverability of both CFA uplift and ATE insurance premiums in all types of civil litigation, including insolvency, with the potential to affect cases that were commenced many years ago and also cases that are yet to be issued.

The root of the problem is the underlying legislation[4] permitting CFA uplift and ATE insurance premiums to be recovered from the losing party. The basic argument is that the losing party's liability for costs, exacerbated very substantially by the CFA uplift and ATE insurance premium, could amount to a breach of Article 6 of the European Convention on Human Rights ("ECHR") regarding the right to a fair trial. If the effect of that legislation is to produce a result which breaches the ECHR then the legislation itself could therefore be unlawful.

For most types of civil litigation CFA uplift and ATE insurance premiums have ceased to be recoverable from the losing party if they post-date 1st April 2013, but insolvency litigation was made an exception for public policy reasons. That exception is subject to review in April 2015.

The Supreme Court has adjourned the appeal hearing to enable the Government to be represented. If the relevant legislation is declared incompatible with the ECHR[5] then there could be a number of fairly major consequences:-

1. The exception for insolvency litigation which makes CFA uplift and ATE insurance premiums recoverable from the losing party would fall away (R3[6] is of course already campaigning for this to survive beyond the 2015 review);

2. The decision would have retrospective consequences. Older CFAs and ATE insurance policies (i.e. pre-1 April 2013) will be affected because the court will no longer be able to order the CFA uplift and ATE insurance premiums to be paid by the unsuccessful party due to the relevant legislation having been found to be incompatible with the ECHR;

3. Any CFA success fee and ATE insurance premium will then have to come out of recoveries or existing assets (if sufficient and where the litigation was properly sanctioned) and if they cannot then there may be some difficult discussions between the relevant lawyers, insolvency practitioners and the creditors; and

4. The Government may be obliged to compensate any losing party who has been ordered to pay CFA uplift or an ATE insurance premium in the past under legislation that breaches the ECHR.

Point 4 alone may cause their Lordships to try hard to avoid a finding of incompatibility with the ECHR, although it is clear that they were very concerned by not only the level of costs in this case but also the distorting effect[7] of the CFA uplift and ATE insurance premium, which when combined could be ruinous for the losing party. The argument clearly gained sufficient traction to merit detailed consideration at an adjourned hearing. Furthermore the fact that the recoverability of both CFA uplift and ATE insurance premiums has fairly recently been abolished in most new cases (but not insolvency) may make having any remaining exceptions to that position hard to justify.

One option might be for their Lordships to find scope within the existing legal framework for the Court to be able to consider the total costs, inclusive of CFA uplift and ATE insurance premium, when considering proportionality. However this may be impossible due to the current formulation of the relevant Civil Procedure Rules.[8]

It is not clear how long it is likely to take for the Supreme Court to clarify the position.

Going Forward

Nothing has changed as yet, but the future for existing CFA funded and ATE insured claims by insolvency practitioners has arguably become uncertain and may remain so for some time to come. In the meantime Insolvency Practitioners may want to consider the potential financial outcome of any litigation currently or about to be conducted under a CFA or with ATE insurance. For instance:-

1. How will the potential outcome for creditors look if the CFA uplift and ATE insurance premium are not paid by the losing party and have to come out of recoveries or the existing funds in the insolvency?

2. Does the insurance premium accrue in stages so that early settlement results in a reduced premium which increases the nearer the case gets to trial?

3. If the CFA uplift and the ATE insurance premium are not recoverable from the losing party and other recoveries are minimal, how will they be paid at all? While the solicitors may be prepared to take a commercial view on their CFA, the ATE insurer may not be so sympathetic.

4. In a case where there might be insufficient funds available even if the case is won, it may be that the only way to avoid all risk of having to pay the ATE insurance premium (if the losing party is not required to pay it because the Supreme Court decides that it should not be recoverable) would be to abandon the claim now so that it never becomes payable[9], assuming that the ATE insurer will permit that to happen and still pay out in respect of the other side's costs.

The comments in this Guidance Note are of a general nature only. Full advice should be sought on any specific problems or issues

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[1] Conditional Fee Agreement i.e. the liability to pay a fee for the legal advice is conditional upon success (as defined in the agreement) in the court proceedings. In the event of success the lawyers are entitled to charge an uplift of up to 100% on top of their basic hourly rate and that uplift is to be paid by the losing party.

[2] "After The Event", referring to the fact that the policy was taken out after the event giving rise to the claim. The policy will then cover the exposure of the insured party in respect of the other side's legal costs and disbursements in the event that the claim fails.

[3] http://supremecourt.uk/decided-cases/docs/UKSC_2012_0076_Judgment.pdf (see paragraphs 32 to 47 of the judgment).

[4] In this case the Courts and Legal Services Act 1990 as amended by sections 27 to 31 in Part II of the Access to Justice Act 1999. This was further amended by sections 44 and 46 of the Legal Aid, Sentencing and Punishment of Offenders Act 2012, but to the extent that CFA uplift and ATE insurance premiums remain recoverable (as they do in insolvency litigation) then the position is unchanged.

[5] In *Callery v Gray* [2002] 1 WLR 2000, the House of Lords effectively confirmed that, subject to reasonableness, success fees and ATE premiums were recoverable. In *Campbell v MGN Ltd (No 2)* [2005] 1 WLR 3394, the House of Lords held that the 1999 Act costs recovery regime did not infringe Article 10 of the ECHR. However, since then the ECHR has criticised the position under English law, albeit in a slightly different context (see *MGN Limited v United Kingdom* (2011) 53 EHRR 5) so the point remains highly arguable.

[6] The Association of Business Recovery Professionals.

[7] Many ATE insurance policies have a deferred and insured premium, meaning that for no initial outlay the combination of a CFA and ATE insurance can result in effectively "risk free" litigation – there is no exposure to the other side's costs due to the ATE insurance cover and so no incentive to keep costs down; in the event of success the losing party pays for the costs, including CFA uplift of up to 100% and the ATE insurance policy premium; and if the claim is lost then there is nothing to pay under the CFA or the ATE insurance policy. This issue is touched upon at paragraph 37 of the judgment.

[8] CPR44 PD paragraphs 11.8 to 11.10 limit what the Court can take into account when considering whether the uplift or the ATE insurance premium is reasonable. Indeed paragraph 11.9 expressly prohibits consideration of whether the costs once uplifted appear disproportionate.

[9] This is on the basis that most ATE insurance policies are self-insuring i.e. there is no premium payable by anyone if the claim fails.