Milbank

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CONTACTS

Tom Canning
Partner
+44-20-7615-3047
tcanning@milbank.com

Andy Levett
Associate
+44-20-7615-3091
alevett@milbank.com

Litigation & Arbitration Group Client Alert: Security for costs – recent developments

The last 18 months has seen several important developments in the case law relating to applications for security for costs. This article seeks to summarise those developments and the circumstances in which an order for security for costs may be available.

INTRODUCTION

An order for security for costs typically protects a party defending a claim (or an appeal), the policy consideration being that a defendant should not be exposed to the risk that it will win at trial and be awarded its costs, but be unable to enforce a costs order against the claimant because, for example, of the claimant's impecuniosity.

An order for security for costs requires a claimant (although sometimes a third party) to provide an acceptable form of security (whether by way of a payment of money into court or bond or guarantee) to meet, if required, the defendant's litigation costs.

An order for security for costs is typically available if **one or more** grounds exist which point to a risk that it will not be possible to enforce a costs order against the party bringing a claim. The primary grounds are contained in CPR 25.13(2):

1. The claimant is resident out of the jurisdiction and outside the states covered by the Recast Brussels Regulation, the Brussels Convention, the 2007 Lugano Convention, or the 2005 Hague Convention (CPR 25.13(2)(a)).

2. The claimant is a company or other body (whether incorporated inside or outside Great Britain), and there is reason to believe that it will be unable to pay the defendant's costs if ordered to do so (CPR 25.13(2)(c)).

3. The claimant has changed its address since the claim was commenced with a view to evading the consequences of the litigation (CPR 25.13(2)(d)).

4. The claimant has failed to provide its address in the claim form or has given an incorrect address (CPR 25.13(2)(e)).

5. The claimant is acting as a nominal claimant, other than as a representative claimant under CPR 19, and there is reason to believe that it will be unable to pay the defendant's costs if ordered to do so (CPR 25.13(2)(f)).

6. The claimant has taken steps in relation to its assets that would make it difficult to enforce an order for costs against it (for example, dissipation of assets or transfer of assets abroad) (CPR 25.13(2)(g)).

However, establishing one of the grounds in CPR 25.13(2) is not enough by itself. The court must also be satisfied "*having considered all the circumstances of the case that it is just to make such an order*" (CPR 25.13(1)).

RECENT DEVELOPMENTS

Interpreting CPR 25.12(1)

CPR 25.12(1) reads "*a defendant to any claim may apply under this Section of this Part for security for his costs of the proceedings*".

In *SARPD Oil International Ltd v Addax Energy and another [2016] EWCA Civ 120*, the claimant brought a claim against the defendant and the defendant looked to 'pass the claim on' by starting a Part 20 claim against a third party (the **"Part 20 defendant"**). The court held that the Part 20 defendant's costs could be treated as the defendant's costs for the purposes of CPR 25.12(1).

The court noted that if the claimant were to lose against the defendant, the defendant would "*very probably*" be ordered to pay the Part 20 defendant's costs as it would have lost its claim against the Part 20 defendant. In all likelihood, the defendant would be able to recover those costs from the claimant, as well as its own costs of defending itself against the claimant and of bringing proceedings against the Part 20 defendant. All of those costs would then become the defendants own costs pursuant to CPR 25.12(1).

But is a defendant able to seek security in relation to costs associated with proceedings that are ancillary to the claim brought by the claimant? The decision in *MA Lloyd & Son Ltd (In Administration) v PPC International Ltd (t/a Professional Powercraft) [2016] EWHC 1583 (QB)* suggests not. In this case, the court held that an application for wasted costs in relation to a claim that had been struck out did not constitute a substantive claim or proceedings, and thus the wasted costs respondent was unable to seek security for costs against the applicant.

So what does constitute a "claim" or "proceedings" for the purposes of CPR 25.12(1)? This question was considered in *Cherkasov and others v Nogotkov Kirill Olegovich [2017] EWHC 756*, a case which concerned an application to set aside the recognition of a Russian insolvency process by the English Courts. In her judgment, Rose J referred

to the views expressed in the leading case in this area (*GFN SA and others v The Liquidators of Bancredit Cayman Ltd [2009] UKPC 39*). In this case, Lord Scott looked at whether interim applications could be deemed proceedings for the purposes of an application for security for cost. He made the distinction between interim applications made for the purpose of regulating the conduct of the parent action, which are not deemed proceedings for the purposes of CPR 25.12(1), and interim applications which raise issues that affect the parties' rights and are independent of the issues in the parent action, which are deemed proceedings. Applying this approach, Rose J deemed that the application to set aside the recognition of the foreign insolvency process did amount to proceedings for the purposes of CPR 25.12(1).

In a case related to the same insolvency process (*In the Matter of Dalnyaya Step LLC sub nom Olegovich v Cherkasov [2017] EWHC 509 (Ch)*), the court held that that an application for security for costs does not operate as a stay on other proceedings. If and when an order for security for costs is made the claim is stayed until the security is provided, but not before then.

Counterclaims

It is possible for a claimant to apply for security for the costs of defending the defendant's counterclaim. The same principles apply in these circumstances as with a standard Part 7 claim, although there are some additional and important considerations.

If the counterclaim and the claim cover identical grounds (i.e. the counterclaim gives rise to the same issues as the claim) then it is likely that the court will consider it unjust to order the defendant to pay security for costs for the claimant to defend the counterclaim (*Physiotherapy Network v Health & Case Management Ltd [2017] EWHC 1238 (QB)*).

However, in *Dawnus Sierra Leone Ltd v Timis Mining Corporation Ltd and another [2016] EWHC B19 (TCC)*, the court held that, when a claim and a counterclaim are independent and both parties are seeking security for costs from the other, "*the appropriate order will ordinarily be that both parties provide security, or that neither party does*".

Stifling a genuine claim

It is long established that:

1. where a claimant's claim is genuine, a court will be reluctant to order a claimant to pay security for costs if doing so is likely to prevent the claim from proceeding;

2. in deciding whether the claim would be stifled, the court will consider whether the claimant can access funds from others to pay the security for costs sum; and

3. the onus is on the claimant to show that the order would stifle the claim.

The decision in *New Tasty Bakery Ltd v MA Enterprise (UK) Ltd [2016] EWHC 1038 (IPEC)* makes it clear that, without evidence that the claimant does not have funds to provide the security sought, and could not obtain them from another source (e.g. a third party who might reasonably be expected to provide funding), the court will be reluctant to accept the argument that the claim would be stifled by a security for costs order.

CPR 25.13(2) – standard of proof for bringing an application

In *Coral Reef Limited v (1) Silverbond Enterprises Limited (2) Eiroholdings Invest [2016] EWHC 874 (Ch)*, the court considered the standard of proof required for CPR 25.13(2)(c). Master Matthews wrote in his judgment "*I have to consider, on the totality of the evidence before the court, whether I am satisfied that there is reason to believe that the Claimant, being a company, will be unable to pay the Defendants' costs if ordered to do so. I do not have to be satisfied that the Claimant will be unable to pay, only that there is reason to believe it. That is a lower standard than, say, the balance of probabilities*".

What might give the court reason to believe a claimant will be unable to pay? In *SARPD*, the court held that, where a claimant is given every opportunity to show it would be able to pay the defendant's costs (if required to do so) and refuses, the court may conclude it would be unable to do so. Here, the claimant had no discernible assets, no published accounts and refused to reveal anything about its financial position.

The court took the same view on the applicable standard of proof in relation to CPR 25.13(2)(a) in *Bestfort Developments LLP and others v Ras Al Khaimah Investment Authority and Others [2016] EWCA Civ 1099*. The correct test is whether there is a real risk of difficulties in enforcing a costs order in the jurisdiction of the claimant and there is no need for the defendant to establish such difficulties on a balance of probabilities test.

After The Event ("ATE") insurance

ATE insurance policies normally cover the legal costs which a claimant is ordered to pay to a defendant should a claim be unsuccessful. The decision in *Premier Motorauctions Ltd and another v PricewaterhouseCoopers LLP & Anor [2016] EWHC 2610 (Ch)* shows that the existence of an ATE policy can, in fact, defeat an application for security for costs. The courts will consider whether the policy is likely to pay out if an adverse costs order is made against the claimant, and if there is no reason to doubt

that it will, or to question the creditworthiness of the ATE insurer, then the security for costs application will likely be refused. There were no such concerns in *Premier Motorauctions* and thus the application for security for costs was indeed refused.

The court's assessment will, however, turn on the terms and context of the policy in question. For example, when deciding if a policy represents reasonably satisfactory security, the court will be interested to know whether there are grounds which justify the insurer avoiding the policy (see *Catalyst Managerial Services v Libya Africa Investment Portfolio [2017] EWHC 1236 (Comm)*) and how the beneficiary/ies of the policy would be treated if the claimant entered insolvency (*Newwatch Ltd and another v Bennett and others [2016] EWHC 3506 (Comm)*).

In *Dunn Motor Traction v National Express [2017] EWHC 228 (Comm)*, the defendant applied for security for costs even though the claimant's sole shareholder had irrevocably indemnified the claimant for any cost liability to the defendant. The claimant argued that this shareholder indemnity was equivalent to an ATE policy and thus the decision in *Premier Motorauctions* should be followed. The High Court held that, whilst ATE insurance was "*a reliable source of litigation funding*", an indemnity from a claimant's shareholder was not. The existence of such an indemnity is only likely to defeat a security for costs application in exceptional circumstances.

Applications against a third party

In a primary litigation (i.e. not an appeal), a defendant may obtain an order for security for costs against a third party to the litigation if:

1. the court, having regard to all the circumstances of the case, considers that it is just to make such an order (CPR 25.14(1)(a)); and

2. either (i) the third party has assigned its right to the claim to the claimant to avoid the possibility of a costs order against it (CPR 25.14(2)(a)); or (ii) the third party has agreed to contribute to the claimant's costs in return for a share of any proceeds from the claim (CPR 25.14(2)(b)).

In the case of *Wall v The Royal Bank of Scotland plc [2016] EWHC 2460 (Comm)*, the court held that if a claimant is being funded by a third party (or there is good reason to believe the same), meaning the court has the power to order security for costs against the third party funder, the court must also have the power to make an order requiring the claimant to reveal the identity of the funder. The power to require the claimant to disclose the identity of the third party funder is necessary to make effective the court's primary power to order security for costs.

The principle from *Wall* was revisited in *The RBS Rights Issue Litigation [2017] EWHC 463 (Ch)*. Here, the court held that a party cannot use an application for

disclosure of the identity of the third party funder in a purely tactical way. The applicant must demonstrate that, following the disclosure, there is a real prospect it will bring an application for security for costs and that there are realistic grounds on which to do so.

In a subsequent judgment (*The RBS Rights Issue Litigation [2017] EWHC 1217 (Ch)*), the court held that when assessing whether an order under CPR 25.14(2)(b) is just, the following factors will be relevant:

1. Whether it is sufficiently clear that the third party is to be treated as having in effect become, in all but name, a real party motivated to participate by its commercial interest in the litigation. The judge made the distinction between those commercial litigation funders acting purely for profit and those acting charitably to enable access to justice (so called "*pure funders*").

2. Whether there is a real risk of non-payment by the third party.

3. Whether there is a sufficient link between the third party funding and the costs for which recovery is sought (i.e. is there some causal link between the funder's conduct and the costs incurred by the defendant).

4. Whether the third party is sufficiently aware of the risk of liability for costs, either by express warning, or by reference to what a party in its position should be taken to appreciate as regards the inherent risks involved. With the growth of third party funding it is assumed that commercial litigation funders do know these risks.

5. Whether there are factors, such as delay in making an application for security for costs or likely adverse effects, which might tip the overall balance against the making of the order.

CONCLUSIONS

The court has a huge amount of discretion when considering an application for security for costs. The recent case law provides significant guidance as to how the court typically exercises this discretion.

LITIGATION & ARBITRATION GROUP

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LONDON

10 Gresham Street, London EC2V 7JD, England

Tom Canning	tcanning@milbank.com	+44-20-7615-3047
Charles Evans	cevans@milbank.com	+44-20-7615-3090
Julian Stait	jstait@milbank.com	+44-20-7615-3005

NEW YORK

28 Liberty Street, New York, NY 10005

Wayne M. Aaron	waaron@milbank.com	+1-212-530-5284
Antonia M. Apps	aapps@milbank.com	+1-212-530-5357
Thomas A. Arena	tarena@milbank.com	+1-212-530-5828
George S. Canellos *Global Head of Litigation*	gcanellos@milbank.com	+1-212-530-5792
James G. Cavoli	jcavoli@milbank.com	+1-212-530-5172
Scott A. Edelman *Firm Chairman*	sedelman@milbank.com	+1-212-530-5149
Christopher J. Gaspar	cgaspar@milbank.com	+1-212-530-5019
David R. Gelfand	dgelfand@milbank.com	+1-212-530-5520
Joseph S. Genova	jgenova@milbank.com	+1-212-530-5532
Katherine Goldstein	kgoldstein@milbank.com	+1-212-530-5138
Robert C. Hora	rhora@milbank.com	+1-212-530-5170
Atara Miller	amiller@milbank.com	+1-212-530-5421
Sean M. Murphy	smurphy@milbank.com	+1-212-530-5688
Daniel Perry *Global Practice Group Leader*	dperry@milbank.com	+1-212-530-5083
Tawfiq S. Rangwala	trangwala@milbank.com	+1-212-530-5587

Stacey J. Rappaport	srappaport@milbank.com	+1-212-530-5347
Fiona A. Schaeffer	fschaeffer@milbank.com	+1-212-530-5651
Jed M. Schwartz	jschwartz@milbank.com	+1-212-530-5283
Alan J. Stone	astone@milbank.com	+1-212-530-5285
Errol B. Taylor	etaylor@milbank.com	+1-212-530-5545
Fredrick M. Zullow	fzullow@milbank.com	+1-212-530-5533

WASHINGTON, DC

International Square Building, 1850 K Street, NW, Suite 1100, Washington, D.C. 20006

David S. Cohen	dcohen2@milbank.com	+1-202-835-7517
Andrew M. Leblanc	aleblanc@milbank.com	+1-202-835-7574
Michael D. Nolan	mnolan@milbank.com	+1-202-835-7524
Aaron L. Renenger	arenenger@milbank.com	+1-202-835-7505

LOS ANGELES

2029 Century Park East, 33rd Floor, Los Angeles, CA 90067

Robert J. Liubicic	rliubicic@milbank.com	+1-424-386-4525
Jerry L. Marks	jmarks@milbank.com	+1-424-386-4550
Mark C. Scarsi	mscarsi@milbank.com	+1-424-386-4580