As Third-Party Class Action Funders Make Their Mark in Canada, An Ontario Court Establishes Some Ground Rules

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- Over the past few years, third-party litigation funding – including funding by major international litigation funders – has become increasingly common in class actions litigation in Canada.
- In a recent decision, *Houle v. St. Jude Medical Inc.*, the Ontario Superior Court of Justice summarized the current state of the law regarding litigation funding agreements.
- The decision is one of the first to address the interplay between the Law Foundation of Ontario's Class Proceedings Fund[1] and private third-party funding agreements, referring to the rules relating to the Fund to limit (by analogy) a third-party funder's contingency fee to 10%, with amounts greater than 10% being subject to Court approval.

Background

The plaintiffs commenced a class action on behalf of all people in Canada who were implanted with certain cardiac defibrillators manufactured by the defendant, St. Jude Medical Inc. The allegations were that St. Jude had:

1. Negligently designed, developed, manufactured and distributed several models of the defibrillators; and
2. Failed to warn its customers of the potential defects once they were known.

Agreements with Counsel and the Third-Party Funder

The representative plaintiffs retained counsel under a contingency fee arrangement that originally specified that class counsel were to receive 33% on a contingency basis. However, class counsel decided that they did not want to be responsible for disbursements and any potential adverse awards of costs. As a result, those issues were dealt with in a separate litigation funding agreement between the representative plaintiffs and Bentham IMF Limited, a global litigation financier. Bentham agreed to pay, on a non-recourse basis:

1. Disbursements incurred by class counsel up to a prescribed maximum amount, after which amount, class counsel would fund the disbursements;
2. Any adverse costs awards against the representative plaintiffs;
3. Any security for costs; and
4. 50% of the reasonable docketed time of class counsel, up to a prescribed maximum amount. (The Court noted that this clause effectively created a very unusual "hybrid" retainer whereby

class counsel was paid 50% of their fees on a non-contingent basis and the remaining 50% on contingency.)

In exchange for the funding, Bentham would receive between 20%-25% of the litigation proceeds with class counsel receiving between 10%-13% of such proceeds, depending on when the litigation was resolved. This arrangement (which superseded the 33% arrangement in the retainer) had the unusual feature of allocating more of the litigation funding to the third-party funder than it did to class counsel (typically it is the other way around).

Approving a Funding Agreement: What the Court Will Consider

In considering whether to approve the funding agreement, the Court concluded that the "general test for determining whether to approve a third-funding [sic] agreement is that the agreement should not be champertous or illegal and it must be a fair and reasonable agreement that facilitates access to justice while protecting the interests of the defendants."

The Court identified seven prerequisites for approval of a litigation funding agreement in the context of a class action proceeding:

1. The procedural, technical, and evidentiary requirements that enable the Court to scrutinize the funding agreement must be satisfied. In assessing this, the Court will consider, among other things, whether (i) the representative plaintiffs received independent legal advice, (ii) the retainer and third party financing agreement were disclosed to the Court and/or defendant; (iii) the third party financier is willing to provide security for costs; and (iv) the background factual circumstances are proffered to the Court;
2. Third-party funding must be necessary. Absent necessity, a funding agreement will not be approved;
3. The third-party financier must make a meaningful contribution to access to justice or behaviour modification. In essence, the funding must be sufficient to achieve the goals of the class action regime or administration of justice;
4. The third-party financier must not be overcompensated or unduly rewarded in the particular circumstances;
5. The third party financier must not interfere with the lawyer-client relationship, the lawyer's duty of loyalty and confidentiality or the lawyer's professional judgment and carriage of the litigation on behalf of the representative plaintiff or class members;
6. The litigation funding agreement must contain a term that the third-party financier will be bound by the deemed undertaking rule and will be bound not to disclose confidential or privileged information; and
7. The litigation funding agreement must not be illegal.

Application to this Case

Applying these factors to the proposed funding agreement, the Court determined that the proposed funding agreement risked overcompensating Bentham (point 4, above) and interfered with the representative plaintiffs' lawyer-client relationship (point 5, above):

- With respect to overcompensation, the Court expressed concern that Bentham's recovery was uncapped and that the amount of its recovery would be unknown until the final determination of the dispute when the amount of litigation proceeds is ultimately determined.
- The Court was of the view that the lawyer-client relationship was undermined by the Bentham agreement, which gave the impression that "the Houles and Class Counsel have promised to prosecute the proposed class action as much, if not more, on behalf of Bentham than on behalf of the Class Members."

While it passed the other tests, the inadequacy of the agreement with respect to points 4 and 5 meant that the Court was not prepared to approve the agreement in its current form.

However, the Court advised the parties that it was willing to approve the agreement if Bentham made certain amendments, such as reducing its share of the contingency fee to 10% - i.e. treating it in the same manner as Ontario's Class Proceedings Fund – and making the balance of its compensation conditional on court approval. The Court reasoned that such an amendment would ensure that Bentham would not be overly compensated as any amounts in excess of the Class Proceedings Fund would be subject to Court approval.

Key Conclusions

Houle is instructive on the parameters and structure of acceptable third party funding agreements in Canada and how the practices of international litigation financiers may need to be adjusted for the Canadian class proceedings environment.

Specifically, the decision provides:

- That the financier's contingency fee should not be greater than 10% unless any excess amounts are subject to Court approval; and
- That the financier cannot, expressly or impliedly, usurp control or carriage of the litigation from the representative plaintiff(s).

[1] The Ontario Class Proceedings Fund is an Ontario based fund that serves to provide financial support to certain approved class actions plaintiffs and indemnifies such plaintiffs for costs that may be awarded against them. In exchange for this financial aid, the Class Proceedings Fund is entitled to an unadjustable levy in the amount of 10% of any litigation proceeds in favour of the plaintiffs plus reimbursement for any funded disbursements.