

Damages-based agreements and termination: a small chink of light

by Maura McIntosh Professional support consultant at Herbert Smith Freehills

Status: Published on July 27, 2020 | Jurisdiction: England, Wales

This article was first published by Practical Law on the Practical Law Dispute Resolution Blog, the predecessor to the Practical Law Dispute Resolution Column which can be found at: uk.practicallaw.thomsonreuters.com/w-038-8059
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[Damages-based agreements \(DBAs\)](#) have been available to fund civil litigation in England and Wales since 2013, when they were introduced as part of the [Jackson reforms](#). But in practice, they are still a rare breed. The reluctance on the part of the legal profession to embrace DBAs is generally attributed to difficulties with their implementation, and in particular the [Damages-Based Agreements Regulations 2013](#) which govern the regime.

The DBA Regulations are (ostensibly) highly restrictive, not least in appearing to ban “hybrid” arrangements which combine a DBA, under which the lawyer receives an agreed percentage of any recovery in the event of success, with some other form of funding, such as a reduced hourly rate which is payable win or lose. This means that, if a lawyer agrees to act under a DBA, it must be a full “no win no fee” agreement, which obviously increases the level of risk for the lawyer. The other key difficulty is the opaque manner in which the DBA Regulations are drafted, which means that in many respects it is simply unclear what is or is not permitted under the regime. And since the price of getting it wrong is an unenforceable fee agreement, with no clear entitlement to a quantum meruit for what may, in many cases, be a very significant amount of work done, that is too great a risk for many practitioners.

One of the areas that has caused some confusion is whether a DBA can include a clause providing for payment on some other basis (for example, hourly rates) if the DBA is terminated, or whether including such a term will render the DBA invalid. This issue has come up in at least two cases I’m aware of: one in which I was part of the team representing solicitors and counsel whose DBA was challenged on this basis (among others), but the case [settled](#) before judgment; and another in which judgment has recently been given on the point, *Lexlaw Ltd v Zuberi*, as considered further below.

Attempts at reform

The difficulties with the DBA Regulations have long been recognised, and there have been various attempts to put them right.

The first was a review conducted by a Civil Justice Council (CJC) working group, at the request of the Ministry of Justice (MoJ). The group was chaired by Professor Rachael Mulheron of QMUL, and I was also a member. Its report published in September 2015 made 45 recommendations on issues of both drafting and policy, as discussed in [my post](#) on this blog at the time. Unfortunately, despite having initiated the review, the MoJ did not act on the CJC’s report. In any event, that report did not include any recommendations regarding termination of DBAs, merely noting the working group’s view that the ability to draft a suitable DBA gave the lawyer sufficient protection against inappropriate termination by the client. In other words, it assumed there was nothing to prevent the lawyer including such a clause without affecting the validity of the DBA.

The next opportunity for reform was the MoJ’s [post-implementation review](#) of the legislation which implemented DBAs, Part 2 of the Legal Aid, Sentencing and Punishment of Offenders Act 2012 (LASPO). In its report published in February 2019, the MoJ accepted that the DBA Regulations would benefit from additional clarity and certainty. It said it would give careful consideration to the way forward in the light of the outcome of an independent review of the drafting of the DBA Regulations which was being undertaken by Professor Mulheron and Nicholas Bacon QC.

Their proposed re-draft of the DBA Regulations was presented at a conference in October 2019 and was broadly welcomed by practitioners. As noted in [my blog post](#) at the time, as well as proposing an end to the ban on “hybrids”, the re-draft addresses the lack of clarity as to what terms can be agreed to apply on termination of a DBA. As a default position, the re-draft provides that the lawyer can charge [costs](#), expenses and counsel’s fees if the client terminates, or if the lawyer terminates where the client has behaved unreasonably, subject to alternative terms being agreed in the DBA.

A supplementary report is currently being prepared to take account of feedback received on the

proposed re-draft. It is due to be submitted to the MoJ by the end of September.

Lexlaw v Zuberi

So against that background, how does *Lexlaw v Zuberi* fit in?

Lexlaw entered into a DBA with its client, Mrs Zuberi, relating to the pursuit of her claims against certain banks alleging mis-selling of derivative products. The DBA provided, at clause 6.2, that if Mrs Zuberi terminated the agreement, she would be liable to pay Lexlaw's time costs, plus expenses, up to the date of termination.

Mrs Zuberi sought to terminate Lexlaw's retainer after a meeting in which the banks indicated that they would make a substantial offer, but Lexlaw did not accept the termination as bringing the DBA to an end. The banks subsequently made an offer which Mrs Zuberi accepted, and Lexlaw brought an action seeking payment of some £125,000 which it said was due under the DBA.

Mrs Zuberi argued that the DBA was unenforceable due to the termination provision at clause 6.2. This was said to be in breach of regulation 4(1) which provides that a DBA must not require the client to pay anything other than the DBA "payment" (that is, the percentage share of damages the client agrees to pay the lawyer under the DBA) and the expenses incurred by the lawyer, in each case net of sums recovered from the losing opponent. Since clause 6.2 required the client to pay time costs on termination, it was said that the DBA was in breach of regulation 4(1) and therefore the DBA was unenforceable. It did not matter that Lexlaw was not actually seeking payment under clause 6.2; its presence in the DBA rendered it invalid.

The High Court's decision

This question was tried as a preliminary issue, with the High Court's judgment handed down on 10 July 2020. The court (HHJ Parfitt sitting as a High Court judge) dismissed Mrs Zuberi's argument, finding that regulation 4(1) does not prevent an agreement under which the lawyer is entitled to time costs if the DBA is terminated before a right to share in the proceeds of the litigation has arisen.

The court appears to have been swayed in particular by the fact that the DBA Regulations contain specific provisions regulating what the lawyer can charge on termination of a DBA in an employment matter, but are silent on this point for DBAs outside the employment sphere. During consideration of the

proposed DBA Regulations in the House of Lords, it was explained that the government considered detailed safeguards relating to termination were needed in the employment context, since employment matters may be undertaken by unregulated individuals, but not in mainstream civil litigation which can only be undertaken by lawyers. Against that background, it is unlikely that the government intended the DBA Regulations to prohibit a term providing for payment of time costs on termination in the civil litigation context.

In essence, in *Lexlaw*, the court held that the purpose of regulation 4 is to prescribe the maximum amount and calculation method of the lawyer's DBA "payment", that is, the lawyer's percentage share of damages under the DBA. It therefore construed regulation 4 as being limited to situations where there is a sharing of the spoils of the litigation between client and lawyer. As the judge put it:

"... if the legislature considered it necessary that damages-based agreements should prevent the solicitor recovering time costs in any circumstances other than when the agreement continued to apply at the conclusion of successful litigation then it would have said so in terms and not as a side consequence of addressing a different subject – how sharing the spoils should work".

Some hope for hybrids?

As mentioned above, the proposed re-draft of the DBA Regulations which was put forward last year by Rachael Mulheron and Nick Bacon provides for the removal of the ban on hybrids. Under the proposals, if the client receives no financial benefit from the litigation, the lawyer can still be paid a fee of up to 30% of irrecoverable costs, so that a DBA is not restricted to a "no win no fee" arrangement. This would obviously go some way to reducing the risks for a lawyer considering taking on a case under a DBA.

Interestingly, the court's interpretation of regulation 4 in *Lexlaw* would appear to support an argument that this sort of hybrid arrangement is in fact permitted under the current DBA Regulations, even without the amendments set out in the proposed re-draft. If the only purpose of regulation 4 is to determine the maximum amount and calculation method of the DBA "payment", and it is solely concerned with regulating the sharing of spoils of successful litigation, then arguably it has nothing to say about what can be paid to the lawyer where there are no spoils to share.

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There would, however, be obvious risks for any law firm testing the point, given the potential for being left with an unenforceable DBA if the court disagrees.

The future of DBAs

After September, once Rachael Mulheron and Nick Bacon's supplementary report has been submitted, it will be for the MoJ to decide on next steps. One hopes that the current proposals for DBA reform will be met with greater enthusiasm, and more action, on the part of the government, than previous attempts at reform.

Of course, it would not be surprising if DBA reform is not at the very top of the government's priority list, while it is grappling with [COVID-19](#) and [Brexit](#) issues, so on any basis it seems likely that there may be some delay before the difficulties with the DBA Regulations are finally addressed. Personally, I am holding out hope for 2021 (in relation to DBA reform and in many other areas, after the general doom and gloom that has been 2020 so far).

In the meantime, when it comes to DBAs, the High Court's decision in *Lexlaw* provides welcome clarity on this one aspect, subject of course to any appeal that might be brought by Mrs Zubairi.

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