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Comparative Legal History

ISSN: (Print) (Online) Journal homepage: https://www.tandfonline.com/loi/rclh20

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To cite this article: Willem H. Van Boom (2020) Insuring vs. investing in litigation: a comparative legal history of litigation insurance and claim investment, Comparative Legal History, 8:1, 2-26, DOI: 10.1080/2049677X.2020.1768255

To link to this article: https://doi.org/10.1080/2049677X.2020.1768255

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Published online: 26 May 2020.

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Comparative Legal History, 2020
Vol. 8, No. 1, 2–26, https://doi.org/10.1080/2049677X.2020.1768255

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Insuring vs. investing in litigation: a comparative legal history of litigation insurance and claim investment

Willem H. Van Boom *

Today, liability insurance and legal expenses insurance are generally accepted as benefits to the society and the idea of insuring against litigation risks does not repel us. In the past, however, it was held that such litigation insurance was fuelling litigation at best or going against good morals at worst. What are the reasons behind this? And how does this compare to the legal history of investment in litigation gains? Claim investment has been frowned upon for centuries and today a dismissive narrative continues to dog this 'product'. So, the legal discourses surrounding insurance and claim investments have developed in different directions. How can this be possibly explained? This paper attempts to answer these questions by comparing the historical developments within European jurisdictions of the concept of insurance against litigation loss and that of the concept of litigation investment. Thus, it aims to improve our understanding of historical paths of both phenomena.

Keywords: usury; champerty; insurance; contingency fee

I. Introduction

A decision to lodge a claim in court or to defend against a claim, is a decision made under uncertainty: the costs are uncertain, and the outcome is uncertain. So, risk averse claimants and defendants may have reasons to look elsewhere – either in advance or as the case arises – for someone willing to bear the financial risks involved. For the claimant, such cost may include attorney fees, court fees, possibly a counterclaim for adverse costs in case the claim is dismissed,[1] and other costs. For the defendant, similar risks apply and the award of the claim itself is

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[1]The 'loser pays' rule, which dates as far back as Justinian times (James A Brundage, 'The Profits of the Law: Legal Fees of University-Trained Advocates' (1988) 32 *American Journal of Legal History* 1–15, 9), leads to an adverse costs order against the losing litigant. Today, it applies in many jurisdictions but varies in extent (ranging from orders for the payment of full and unabated costs and expenses incurred by the victorious litigant to fixed or tariffed cost orders). On costs and cost shifting rules, see, with further references, Willem H Van Boom, 'Litigation Costs and Third-party Funding' in Willem H Van Boom (ed), *Litigation, Costs, Funding and Behaviour – Implications for the Law* (Routledge, 2017) 5–30.

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an additional risk. For either parties, entering into a private insurance contract may help to shift these risks to a risk-neutral risk bearer. For claimants, there is the additional possibility of finding someone willing – after the claim has arisen – to invest in the claim by sharing in the litigation risks or having these risks fully transferred to him in return for a share in the proceeds (if and when they accrue). Apart from risk aversion, there is an issue of access to justice. Some individuals just do not have the money to pay for a lawyer to start with. Nowadays, private legal expenses insurance (hereafter: LEI) and state-funded legal aid, where available, cater in part to the needs of these impecunious litigants.[2] Until the surge of the welfare state post-World War II, the poor had to rely on the church, guilds, unions, charity and poor relief for legal support. For them, there was no access to the markets for litigation risk transfer anyway.

So, the decision to seek insurance or investment, and enter into a contract for the transfer of the litigation risk, sounds much like a rational decision made by competent actors on a free and efficient market for litigation risk transfer. And that is exactly what it might be in a purely economic context, devoid of any religious, cultural or legal influences. However, when we look at the historical developments of litigation insurance and claim investment, the emerging picture is one of a market shaped and moulded by those exact influences. In today's Western societies, the benefits of insurance contracts against the risks of litigation are widely acknowledged. Liability insurance usually covers the insured against both the risk of losing a case and the cost of defending the claim. LEI covers the expenses of litigating a claim as such. In contemporary terms, liability insurance and legal expenses insurance are generally accepted as benefits to the society and the idea of *insuring against litigation risks* does not repel us. Such insurance contracts are neither illegal nor against good morals. In the not so distant past, however, it was sometimes held that such litigation insurance was fuelling litigation at best or going against good morals at worst. What are the reasons behind this? And how does this compare to the legal history of investment in litigation gains? Such claim investment arrangements can be found in legal systems which allow 'no cure no pay' contingency fees for attorneys, third-party litigation funding and similar instruments of 'litigation investment'. Claim investment has been frowned upon for centuries and to this day, a dismissive narrative continues to dog this 'financial product' in certain jurisdictions. Effectively, claim investment contracts continue to be far more contested than liability insurance and LEI are. How can this difference in historical paths between litigation insurance and claim investment be explained?

This contribution attempts to address these issues from a comparative legal historical perspective. It does so by comparing earlier and more recent

[2] A brief introduction to the concept of legal aid can be found at Bernard Hubeau and Ashley Terlouw, 'Legal Aid and Access to Justice: How to Look at and Evaluate Legal Aid Systems?' in Bernard Hubeau and Ashley Terlouw (eds), *Legal Aid in the Low Countries* (Intersentia, 2015) 3–14.

developments in common law with continental European jurisdictions and by focussing on the degree of acceptance in the legal discourse of the concept of insurance contract coverage against litigation loss and the concept of litigation investment contracts. Thus, this contribution aims at improving our understanding of the historical paths of both phenomena and in doing so, it may also provide clues for divining future developments. The structure is as follows. First, two general issues of contract validity, namely *alea* and *usury*, are briefly introduced (Section II). As will become apparent, the discourse surrounding wagering and usury play a pivotal role in the development of the law concerning litigation insurance and claim investment. Thereafter, an outline of the development of litigation insurance is provided (Section III), followed by an overview of the development of claim investment by attorneys and third parties (Section IV). It concludes by contrasting the two distinct historical paths and providing clues as to possible explanations behind their different trajectories (Section V).

II. The trouble with *alea* and *usury*

Before we delve into more details of contracts for litigation risk transfer, there are two 'background' variables that must be introduced: the ambiguous relationship of law and religion with aleatory contracts (contracts involving chance) and the difficult relationship with usury, the business of making money by lending money against interest.

Over the centuries, *aleatory* contracts[3] – where one or either party is under a conditional obligation to perform on the happening of a future uncertain event – have been treated with suspicion.[4] The scope, nature, and productivity of these contracts, however, vary considerably. Wagering and betting are aleatory as much as insurance, bottomry, annuities and tontines,[5] and more modern contracts

[3]Until 2016, art 1964 Code Civil (1804) described and listed the *contrat aléatoire* (aleatory contract). Literally, 'aléatoire' (which stems from the Latin *alea*, meaning both dice and chance, fortuity) refers to randomness and chance events. Art 1964 provided:

> The aleatory contract is a reciprocal agreement whose effects, as to advantages and losses, depend upon an uncertain event, either for all the parties, or for one or several of them. Such contracts are: Insurance contracts, Bottomry, Gaming and betting, Contracts for life annuity.

With the 2016 reform, art 1964 Code Civil was replaced by art 1108 which merely provides the definition that a contract is aleatory where the parties agree that the effects of the contract – both as regards its resulting benefits and losses – shall depend on an uncertain event.

[4]This remains the case today: in many countries, gaming and wagering debts are unenforceable in civil law unless regulated by public law.

[5]The tontine is an annuity-type contract and was used both by public entities such as states and cities to raise capital as well as by groups of individuals (churches, guilds) to offer

such as futures, derivatives and the like. Yet, the question is whether they should be tarred with the same brush of illegality and unenforceability? For centuries, lawyers and theologians have grappled with the question. For instance, the Romans found that wagering contracts were valid, but some forms of gaming were not.[6] In later times, Christian faith and legal authorities were more inclined towards rejecting frivolities such as gaming and betting.[7] However, distinguishing frivolity from societally productive 'financial products' such as insurance proved to be difficult. As a result, the position of the law concerning aleatory products remained *ambivalent* for a prolonged period of time. In fact, life insurance was long seen as going against religious and legal principles because it constituted betting on lives.[8] So, insurance and wager were not always clearly distinguished until the doctrine of 'insurable interest' took root and the risk transfer rationale of insurance became more pronounced.[9] Also, in our modern eyes, the treatment of aleatory contracts was unprincipled, and in some instances outright hypocritical. For instance, the disapproval of wagering did not stop sovereigns from monopolizing lotteries and exploiting them as a welcome capital source for the treasury coffers.[10]

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mutual financial protection. See Phillip Hellwege, *A History of Tontines in Germany – From a Multi-purpose Financial Product to a Single-purpose Pension Product* (Duncker & Humblot, 2018) 156; Herman Wagenvoort, *Tontines – Een onderzoek naar de geschiedenis van de lijfrenten bij wijze van tontine en de contracten van overleving in de Republiek der Verenigde Nederlanden (diss Utrecht)* (1961) 115.

[6]Marinus Theodorus Goudsmit, *Het begrip en wezen der kansovereenkomsten (diss Leiden)* (WT Werst, 1871) 51–121; Johan Petrus Van Niekerk, *The Development of the Principles of Insurance Law in the Netherlands from 1500 to 1800 (Vol I)* (Juta, 1998) 120.

[7]Hugo Grotius, *Inleiding tot de Hollandsche rechts-geleertheid* (Wouw, 1631) III 3.48–49 held that wagers were against the common good and therefore unenforceable.

[8]See, eg, Van Niekerk (n 6) 119–21; Sinem Ogis, *The Influence of Marine Insurance Law on the Legal Development of Life and Fire Insurance in England* (Duncker & Humblot, 2019) 129–60.

[9]Sigismundus Scaccia 1619, as discussed by Guido Rossi, 'Civilians and Insurance: Approximations of Reality of the Law' (2015) 83 *Tijdschrift voor Rechtsgeschiedenis* 323, 346–47. By the 1700s, financial products such as *futures* were also accepted as legitimate, at least in those countries where mercantile culture had become dominant. See Nicolas Magens, *An Essay on Insurances (Vol I)* (J Haberkorn, 1755) 29:

> Merchants may be allowed to try their Skill in judging or conjecturing about the Rise or Fall of the Price of any Commodity, provided no Prejudice arise from it to the Publix, nor any Frauds be committed. A Covenant of this Nature may be called a Wager, rather than an Insurance.

[10]For example, the nineteenth century Dutch statesman Thorbecke complained that state-run 'hazard games' which were only designed by the State to collect money and that they opposed all healthy ideas of 'seemliness and economy'; see Remieg Aerts, *Thorbecke wil het – Biografie van een staatsman* (Prometheus 2018) 150.

In sum, the aleatory contract was fraught with the risk of illegality and unenforceability. For slightly different reasons, similar risks played a role in relation to usury. To avoid misunderstanding, it is essential to appreciate that the term *usury* itself may mean different things, depending on context and jurisdiction. Originally, it signified money given as a remuneration for the use of money, in addition to the payment of the principal sum borrowed. In more modern terms, it may refer to the act of charging an interest rate above a statutory limit.[11] Also, the adjective 'usurious' is sometimes used to denote any unbalanced or asymmetrical contract where one party extracts an excessive profit to the detriment of the other party.[12]

The idea that a moneylender charges interest seems self-evident to modern western society, but in religious societies of our western past, that was not always the case. In fact, for several centuries there was no place for *interest* in the relationship between people, their faith and culture. This relationship was such that people were deemed to be connected to their God and fellowmen more than to their goods and their money, and that wages or profits were primarily considered the fair reward for the labour of making a living. The concept of making your money work for you or striving for excessive profits was in conflict with society's preconception of a spiritually enriched life.[13] In this respect, a straight line can be drawn from Aristotle, who firmly rejected the hoarding of money as unproductive *χρηματιστική*, to theologian Thomas Aquinas and his dislike for 'usury', making money by lending money and charging interest on money loans. The latter stood firmly on the catholic tradition which relied on several scriptures to ban and repress 'usury'.[14] However, the interpretation of the Bible and the implications derived from it varied over time.[15] In the Middle Ages, canon law as applied by ecclesiastical courts, upheld a complete prohibition of any kind of usury.[16] Money was considered 'naturally barren' and merely meant to serve purposes of exchange; making it breed money was held to be a perversion

[11]Cf James Birch Kelly, *A Summary of the History and Law of Usury, with an Examination of the Policy of the Existing System, and Suggestions for its Amendment together with a Collection of Statutes* (Johnson, 1853) 13.
[12]Luther referred to 'asymmetrical bargains' as a category of usurious contracts (Philipp Robinson Rössner, *Martin Luther – On Commerce and Usury (1524)* (Anthem Press, 2015) 99); the concept seems related to the *iustum pretium* concept. Cf William Boyd, 'Just Price, Public Utility, and the Long History of Economic Regulation in America' (2018) 35 *Yale Journal on Regulation* 721, 731–32.
[13]Rössner (n 12) 122.
[14]See generally Kelly (n 11) 1–33.
[15]See the overview by Ingeborg Haazen, 'Rente en risico: de ontwikkeling van zeeleen naar verzekering' in Chris Coppens (ed), *Secundum Ius – Opstellen aangeboden aan prof. mr. P.L. Nève* (Gerard Noodt Instituut, 2005) 127–61.
[16]Cornelis Jacob Zuijderduijn, *Medieval Capital Markets – Markets for Renten, State Formation and Private Investment in Holland (1300–1550)* (Brill, 2009) 62–71; Paolo Astorri, *Lutheran Theology and Contract Law in Early Modern Germany (ca. 1520–1720)* (Ferdinand Schöningh, 2019) 324. Cf Warren Swain and Karen Fairweather, 'Usury and the Judicial Regulation of Financial Transactions in Seventeenth- and Eighteenth-century England'

of its constitution and a mortal sin.[17] Whatever was the principled stance taken by theologians, worldly rulers had to deal with practical challenges such as the real societal needs of capital markets. As a consequence, *mutuum* against reasonable interest rates was condoned (if only to ensure that rulers could borrow to literally fill their war chests).[18] Also, the positions taken by theologians and church officials gradually shifted. For instance, the Bible was sometimes interpreted in such a way that it did not prohibit Jews from lending to Christians, and so they did. Also, by the sixteenth century, canon law had slowly lost its grip on private law, culminating in statutes which declared money loans valid provided they stayed within the statutory interest rate caps.[19] Thus, the focus of attention shifted to an appropriate *level* of the interest. Meanwhile, the idea took root that the usury restrictions would not apply if an additional risk premium (*pretium periculi*) was charged whenever such an additional risk was involved.[20] This development first took root in commercial enterprise, the 'marine adventure'. Among merchants, the customs and rules were relaxed far sooner than that of ordinary citizens, usually because the types of contract involved were accepted internationally.[21] This resulted in early recognition of the legality of commercial exchanges for risk transfer such as bottomry, insurance, and (discounting of) bills of exchange.[22]

Later, these changes trickled down to the 'land' economy. Over the centuries, several contract forms evolved which did not sit well with usury restrictions. Their success varied; some were rejected while others became accepted or were at least condoned. The acceptance was dependent on whether the *pretium periculi* was considered genuine or feigned. This resulted in acceptance of contracts in which the lender ran a *risk* beyond the risk of impecuniosity of the borrower, even though the motive of the parties to evade the usury prohibition was sometimes

in Mel Kenny, James Devenney and Lorna Fox O'Mahony (eds), *Unconscionability in European Private Financial Transactions* (CUP, 2010) 148.

[17]Sir William Blackstone, *Commentaries on the Laws of England in Four Books – Book II The Rights of Things* (1766) 458 was unimpressed; he countered the argument of 'barrenness of money' with the example of a house: houses do not bear fruit either, but yet the owner may charge a price for its use (Blackstone followed Hugo Grotius, *De iure belli a pacis* (1625), Book II, Ch XII, § 20: 'the industry of man has made houses, and other things naturally barren, to become fruitful').

[18]Charles R Geisst, *Beggar Thy Neighbor – A History of Usury and Debt* (University of Pennsylvania Press, 2013) 97–136; John H Munro, 'The Medieval Origins of the Financial Revolution: Usury, Rentes, and Negotiability' (2003) 15 *The International History Review* 505, 514.

[19]See the statutes quoted by Kelly (n 11) 67–71.

[20]See, eg, Munro (n 18) 505–62; Haazen (n 15) 129–61; Zuijderduijn (n 16) 62–71.

[21]Eg, Blackstone (n 17) 461 states that bottomry was not in violation of usury restrictions because it was considered valid 'in all trading nations'.

[22]Cf Rössner (n 12) 97.

clear. This opened up possibilities for several contracts such as annuities.[23] Annuities became a popular financial product in the Middle Ages as they opened up the possibility of lending capital at an interest beyond the limits of usury laws. The capital lender 'bought' an annuity from the 'borrower' who did not promise to return the money with interest but instead to pay an annuity (typically an amount x per year) until the death of someone. Usually, the annuity was for the life of the buyer. The amount x would be set at a rate which would clearly contravene usury laws if not for two points of difference between an ordinary money loan and an annuity: with an annuity, the capital sum paid by the buyer as such would not be repaid, and the buyer bore a risk which the lender does not bear: the annuity terminated upon the death of the person whose life it was bought on.[24]

By the 1600s and 1700s, the legal debate had shifted from interest rates on money loans to a more general conceptualization of usury, namely by contrasting *normal* versus *abnormal, usurious* profitmaking. Seemingly following Grotius' nuanced position on usury,[25] Blackstone dryly observed that allowing lenders to charge interest was a commercial necessity: 'Unless money therefore can be borrowed, trade cannot be carried on and if no premium were allowed for the hire of money, few persons would care to lend it'. So over time, a certain remuneration for money-lending services had become acceptable. What remained in the 1700s was a dislike for avaricious profitmaking beyond what was reasonable for a fair and equitable living.[26] The concept of usury had become a general label for the difference between normal, *moderate* profitmaking and *exorbitant* profits:

> To demand an exorbitant price is equally contrary to conscience, for the loan of a horse, or the loan of a sum of money: but a reasonable equivalent for the temporary inconvenience, which the owner may feel by the want of it, and for the hazard of his losing it entirely, is not more immoral in one case than it is in the other. (…) A capital distinction must therefore be made between a moderate and exorbitant profit.[27]

[23]Munro (n 18) 518–62. Another popular contract was the 'post-obit bond' where a borrower receives a sum in return for his promise to pay a (larger) amount if and when he inherits the family fortune. Since his earlier death would prevent any such inheritance, the lender shares in the risk. This was an existing form of credit in the 1600s and courts were split over whether this practice was legal and ethical or not. See Robert Buckley Comyn, *A Treatise on the Law of Usury* (Pheney, 1817) 40; Kelly (n 11) 42–43; Swain and Fairweather (n 16) 157–58. Cf Ciara Kennefick, 'The Contribution of Contemporary Mathematics to Contractual Fairness in Equity, 1751–1867' (2018) 39 *The Journal of Legal History* 307–39.

[24]On whether annuities violated the principle against usury, see, eg, Hellwege (n 5) 150. Interestingly, the 'impenetrable mystery' of the calculations underlying annuities somehow shielded this contract from the *laesio enormis* remedy. See Kennefick (n 23) 310.

[25]Hugo Grotius, *De iure belli ac pacis* (1625) Book II, Ch 12, para 20–22. Grotius concludes that the Dutch custom of charging a maximum of eight percent to ordinary people and 12 percent to traders seem 'not repugnant to any natural or divine right' (para 22).

[26]Rössner (n 12) 89.

[27]Blackstone (n 17) 459. Interest charges were, in other words, a 'fact of life' (Swain and Fairweather (n 16) 149). By the late 1700s, the early modern political economy cleared the

Finally, in nineteenth century Britain, the interest caps were abolished[28] but disbalanced contracts could still be countered by general common law remedies – where available – against fraud, mistake, duress and undue influence. In other legal systems, the concept of usury continued to exist but developed into a doctrine against abuse of economic powers and duress in a narrower sense.[29]

What did all this mean for contracts for transfer of litigation risk? Well, it did not signify at all that such contracts were welcomed and embraced as productive and ethical. As we shall see, doctrines against champerty and maintenance continued to play their role in some countries. What it did indicate, however, was a slowly growing conceptualization of what I would like to call *commodification of risk*: the growing acceptance of the idea that contracts which explicitly shift risks which were considered to be in God's hands, are productive and therefore legally binding and enforceable. For instance, once we accept that money loans with a conditional payment obligation for the borrower are not to be considered usurious because of the contingency element (where someone borrows £20 under the condition he will have to pay the lender £100 upon the happening of some contingency, the contract is not usurious merely because of the *pretium periculi*),[30] then intellectually the next step to allow contracts for litigation risk transfer is not so far away. Interestingly, Martin Luther, the sixteenth century reformist theologian who spoke out against usury as much as he had spoken out against the commodification of indulgences by the church,[31] considered financial products such as annuities to be unethical not only because they circumvented the usury laws, but also because they caused 'asymmetrical bargains' in the sense that only one party ran a risk. In his view, such contracts served to transfer the financial consequences of uncertainty (in annuities, the uncertainty of the date of the death of the person involved) to the debtor of the annuity (at a risk premium). Luther advocated that this one-sided risk transfer be substituted with a risk-sharing

final resistance (see, eg, Jeremy Bentham, *Defence of Usury; Shewing the Impolicy of the Present Legal Restraints on the Terms of Pecuniary Bargains* (Payne and Foss, 1787)).

[28]Usury Law Repeal Act (1854) 17&18 Vict c 90. See William Cornish and others, *Law and Society in England 1750–1950* (Hart Publishing, 2nd edn 2019) 221.

[29]Cf § 138 BGB (1900): (1) Ein Rechtsgeschäft, das gegen die guten Sitten verstößt, ist nichtig. (2) Nichtig ist insbesondere ein Rechtsgeschäft, durch das jemand unter Ausbeutung der Zwangslage, der Unerfahrenheit, des Mangels an Urteilsvermögen oder der erheblichen Willensschwäche eines anderen sich oder einem Dritten für eine Leistung Vermögensvorteile versprechen oder gewähren lässt, die in einem auffälligen Missverhältnis zu der Leistung stehen. Cf art 152 Weimarer Reichsverfassung 1919: Im Wirtschaftsverkehr gilt Vertragsfreiheit nach Maßgabe der Gesetze. Wucher ist verboten. Rechtsgeschäfte, die gegen die guten Sitten verstoßen, sind nichtig.

[30]Cf Rössner (n 12) 153; Astorri (n 16) 340.

[31]Luther's sermon 'On commerce and usury' (1524) was an attack on lending practices and usurious self-enrichment generally. See on Luther's attack on indulgence sales in this context Rössner (n 12) 15–38.

arrangement, where the lender was not entitled to a fixed percentage in interest but shared with the borrower in his fortunes: a good return in good times and less so in bad times.[32] Although Luther may have suggested this merely to drive home a theoretical point, he unwillingly may have suggested accepting a type of risk-sharing which we nowadays can actually witness in litigation funding contracts. To be fair, I am not so confident he would actually have endorsed such contracts.

Having sketched the development of the discourse on *alea* and usury, in the following section we can turn more specifically to the development of legal thinking surrounding insurance as a risk transfer instrument.

III. Insurance against litigation risk

1. *Insurance generally*

Risk creates and socializes responsibility, and insurance can therefore be seen as a form of social responsibility.[33] However, for this to happen, society must identify certain ‘Acts of God’ and the vagaries of life as *risks*, then as *undesirable* risks and finally it must be open to the idea that it is both productive and seemly to take precautionary measures to protect oneself financially against such risks. In western societies, this process took centuries. It was piecemeal in the sense that first, mercantile adventure was defined as a risk that merited contracts for the transfer of risk. Such insurance was an affair for merchants amongst themselves.[34] The risks associated with ‘land’ (‘terrestrial insurance’ as it is sometimes referred to, in contrast with marine insurance) such as building insurance (fire), life insurance and other insurance forms, experienced a different development. Hereafter, it will become apparent that the difference in development between ‘terrestrial’ and marine insurance is highly significant for a proper understanding of the historical pathways of liability insurance and LEI. Therefore, it merits further discussion here. The difference in the said development can be explained by various factors. For terrestrial insurance to become accepted, it had to shed the odium of *usury* and *wagering*.[35] It did so, roughly speaking between the 1600s and 1700s. As far usury was concerned, in marine insurance the path had been prepared by marine loans (*foenus nauticum* and *bottomry*) and the general tendency of the *lex mercatoria* was to ignore canonical dogmas.[36] The association with wagering was more difficult to overcome until the doctrine of insurable interest took a firm hold. The

[32] *Ibid,* 156–57. Cf Igor Van Loo, *Vernietiging van overeenkomsten op grond van laesio enormis, dwaling of misbruik van omstandigheden (diss OU)* (2013) 102.

[33] See, eg, Tom Baker and Jonathan Simon, *Embracing Risk: The Changing Culture of Insurance and Responsibility* (University of Chicago Press, 2002) 33–49.

[34] See, eg, Cornel Zwierlein, *Der gezähmte Prometheus – Feuer und Sicherheit zwischen Früher Neuzeit und Moderne* (Vandenhoeck & Ruprecht, 2011) 50–54.

[35] Rossi (n 9) 325–64.

[36] Martinus Theodorus Goudsmit, *Geschiedenis van het Nederlandsche Zeerecht – Inleiding, Geschiedenis der bronnen* (Martinus Nijhoff 1882) 283.

requirement of insurable interest was the response of the growing practice of people buying insurance policies without having interest in the subject matter.[37] Such practices in life insurance were deemed to be an unethical wagering with death at best and an open invitation to death at worst; that is to say, an invitation for fraudulent behaviour or 'moral hazard' on the part of the policyholder to increase the chances of death of the insured body.[38] For instance, English courts first considered such life insurance practices without the requirement of evidence of a pre-existing 'insurable interest' to be valid and legal, but ultimately they were banned by statute.[39] Thus, for an insurance contract to be binding, the requirement of 'insurable interest' – the fact of some pre-existing relation or concern of the insured in the subject matter of the insurance contract[40] – took root.

Getting rid of the odium of *usury* and *wagering* facilitated the growth of terrestrial insurance markets. Yet other factors also go a long way in explaining the late arrival of markets for private terrestrial insurance contracts,[41] one of these being guilds. Before 1800, many terrestrial risks were spread by guilds and other solidarity and mutual insurance constructs rather than by commercial insurance contracts concluded on competitive markets. While marine insurance developed as a commercial contract as part of an international *lex mercatoria* community, in many European countries the classical types of terrestrial insurance, such as fire and life insurance, usually had their roots in the cooperative and mutual protection provided by 'risk solidarity communities' such as guilds.[42]

[37]Geoffrey Clark, 'Embracing Fatality through Life Insurance in Eighteenth-Century England' in Tom Baker and Jonathan Simon (eds), *Embracing Risk: The Changing Culture of Insurance and Responsibility* (University of Chicago Press, 2002) 82–96.

[38]The argument is posited by several authors; see, eg, Marco Van Leeuwen, *De rijke Republiek: gilden, assuradeurs en armenzorgen 1500–1800* (Zoeken naar zekerheid – Risico's, preventie, verzekeringen en andere zekerheidsregelingen in Nederland 1500–2000, Verbond van Verzekeraars/NEHA, Den Haag 2000) 103.

[39]Life Assurance Act 1774 (14 Geo 3, c 48) for life insurance and Marine Insurance Act 1745 (19 Geo 2, c 37; repealed by s 92 Marine Insurance Act) for marine adventures. Contracts entered into without insurable interest were null and void; see *Allkins v Jupe* (1877) 2 CPD 375 and *Gedge v Royal Exch Association Corp* [1900] 2 QB 214. Cf Timothy Alborn, 'A Licence to Bet: Life Insurance and the Gambling Act in the British Courts' in Geoffrey Clark and others (eds), *The Appeal of Insurance* (Toronto University Press, 2010) 110–26. The requirement of insurable interest is continued in s 4 Marine Insurance Act 1906. See Edward Louis de Hart and Ralph Iliff Simey, *Arnould on the Law of Marine Insurance and Average* (Stevens and Sons | Sweet and Maxwell, 10th edn 1921) 346–465. Cf for a more nuanced analysis Jonathan Gilman and others, *Arnould: Law of Marine Insurance and Average* (Sweet and Maxwell | Thomson Reuters, 19th edn 2018) 352. Interestingly, the 1745 Act did not stand in the way of insurance as a wager concerning foreign vessels; *Thellusson v Fletcher* (1780) 1 Dougl 315.

[40]*Lucena v Craufurd* (1806), 2 B & PNR 269 at 302 (Lawrence J). Cf Gilman and others (n 39) 364.

[41]Also, insurance industry had to develop reliable methods of calculating risk, which depended on several mathematical improvements. See, eg, Kennefick (n 23) 327–39.

[42]For continental Europe, see, eg, Julia Caroline Scherpe, *Das Prinzip der Gefahrengemeinschaft im Privatversicherungsrecht (diss Freiburg)* (Mohr Siebeck, Tübingen 2011)

The Napoleonic era upset the risk distribution in 'terrestrial risks'. Guilds were abolished, but a large-scale insurance industry in the capitalist tradition – apart from the obvious terrestrial insurance product of building insurance against fire risks – had not yet been born. In some countries, this resulted in a continued model of 'guild-like' risk pooling for traditional hazards such as fire, and a slow growth in other insurance products catering for terrestrial trade risks such as liability risks. In others, the demise of guilds was attenuated in part by the rise of voluntary risk pooling.[43] Otherwise, it left a void, given that a wide-ranging commercial insurance industry did not yet exist and was unable to quickly mushroom after the yoke of Napoleon's continental blockade had been lifted. In fact, the post-Napoleonic age coincided with the rise of the legal doctrine of incorporation of enterprises. This prompted national legislatures to introduce incorporation rules and capital requirements for the insurance business which may well have hampered the development of terrestrial insurance markets.[44] The most developed insurance industry of that era, the English, tried to penetrate the new continental markets[45] but their attempts were not always met with a warm

57; Phillip Hellwege, 'A Comparative History of Insurance Law in Europe' (2016) 56 *American Journal of Legal History* 66, 67; Phillip Hellwege, 'Die historische Rechtsvergleichung und das europäische Versicherungsrecht' (2014) 131 *Zeitschrift der Savigny-Stiftung für Rechtsgeschichte (Germanistische Abteilung)* 226, 228–265. See also Sandra Bos, '*Uyt liefde tot malcander' – Onderlinge hulpverlening binnen de Noord-Nederlandse gilden in internationaal perspectief (1570–1820)* (IISG, 1998) 39 on the economic function of Dutch guilds. Note that commercial marine risks were sometimes self-insured through mutual assistance arrangements of guild boxes; see, eg, the Groningen skippers' arrangements (Sabine Go, *Marine Insurance in the Netherlands 1600–1870 (diss VU Amsterdam)* (Aksant, 2009) 36–45). For London and some German cities, it bears mentioning that fire insurance developed as a private contract-based industry (although in many instances in the form of a mutuality), not as a guild-dominated operation. See Peter George Muir Dickson, *The Sun Insurance Office 1710–1960 – The History of Two and a Half Centuries of British Insurance* (OUP, 1960) 1; Robin Pearson, *Insuring the Industrial Revolution – Fire Insurance in Great Britain 1700–1850* (Ashgate, 2004) 62; Zwierlein (n 34) 252–61; Ogis (n 8) 57–64.

[43]See for a picture of the partial transition from the compulsory guild solidarity to a voluntary risk pooling cooperative structure, eg, Joost van Genabeek, *Met vereende kracht risico's verzacht – De plaats van onderlinge hulp binnen de negentiende-eeuwse particuliere regelingen van sociale zekerheid* (IISG 1999) 81.

[44]See, eg, the early Dutch regulation of insurance companies (Koninklijk Besluit 16 July 1830), on which Wagenvoort (n 5) 111–13; Ewoud H Hondius, *Standaardvoorwaarden – Rechtsvergelijkende beschouwingen over standaardisering van kontraktsbedingen en overheidstoezicht daarop (diss Leiden)* (Kluwer, 1978) 378–79.

[45]Phillip Hellwege, 'Die historische Rechtsvergleichung und das europäische Versicherungsrecht' (2014) *Zeitschrift der Savigny-Stiftung für Rechtsgeschichte (Germanistische Abteilung)* 255. See *ibid*, 237 for the example of the entry into the German market of the English commercial fire insurance company Phoenix. For a comprehensive account of the export of the British capitalist insurance industry in the nineteenth century, see Zwierlein (n 34) 315–23.

reception.[46] For instance, when the English insurance company *Phenix* tried to get a foothold in the Netherlands, the government rejected incorporation under Dutch law under the pretence of its products being unethical and dangerous: insurance against theft and burglary would provoke an increase of such crimes.[47] The more plausible reason for the rejection was protection of domestic interests.[48]

Another factor is *wealth*, or rather the absence of it. Terrestrial insurance contracts presume wealth at risk – be it a house, goods in transit or a life. So with the increase in overall middle and lower class wealth in the nineteenth century, demand for insurance products only started to grow well after the Napoleonic havoc had long passed.[49] In most continental European countries, before 1850 such middle class wealth simply did not exist.[50] With the rise of the middle class in second half of the nineteenth century came a growing demand for

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[46]For instance, in the Netherlands the entry of foreign insurance companies onto the Dutch market was actively discouraged and blocked. See Loes van der Valk, 'Overheid en verzekeringsbedrijf 1815–1890' in Jacques van Gerwen and Marco HD Van Leeuwen (eds), *Studies over Zekerheidsarrangementen – Risico's, risicobestrijding en verzekeringen in Nederland vanaf de Middeleeuwen* (NEHA/Verbond van Verzekeraars, 1998) 269. One of the reasons may well have been that until the early 1800s, the sale of life insurance products such as annuities and widowers' funds was not in the hands of commercial insurers, but in the hands of provinces and cities (and guilds). See Ida H Stamhuis, 'Levensverzekeringen 1500–1800' in Jacques van Gerwen and Marco HD Van Leeuwen (eds), *Studies over Zekerheidsarrangementen – Risico's, risicobestrijding en verzekeringen in Nederland vanaf de Middeleeuwen* (NEHA/Verbond van Verzekeraars, 1998) 143–45. The incumbents could well do without commercial insurers on the capital market. Cf Clive Trebilcock, *Phoenix Assurance and the Development of British Insurance – Volume I 1782–1870* (CUP, 1985) 244–45.

[47]'Zoo heeft de Koning (…) Zijne goedkeuring geweigerd aan eene naamlooze maatschappij, ten doel hebbende *de verzekering tegen diefstal en binnenbraak*, – welker oprigting hoogst schadelijk voor de ingezetenen zoude zijn geweest, en die misdrijven niet weinig zoude hebben aangemoedigd. Zoo heeft eindelijk de Regering in der tijd, op verzoek een aandrang van de kamers van koophandel in de Zuidelijke gewesten, zich verzet tegen de toelating van succursale takken der Engelsche assurantiecompagnie *de Phenix* genaamd (…) ten einde de Nederlanders daardoor niet te benadeelen' (Justinus Cornelius Voorduin, *Deel VIII (Geschiedenis en beginselen der Nederlandsche Wetboeken, volgens de beraadslagingen deswege gehouden bij de Tweede Kamer der Staten Generaal; uit oorspronkelijke, grootendeels onuitgegeven staatsstukken opgemaakt en den den Koning opgedragen)* (Geschiedenis en beginselen der Nederlandsche Wetboeken, volgens de beraadslagingen deswege gehouden bij de Tweede Kamer der Staten Generaal; uit oorspronkelijke, grootendeels onuitgegeven staatsstukken opgemaakt en den den Koning opgedragen, Robert Natan 1840) 172–73).

[48]Voorduin (n 47).

[49]Albert Schug, *Der Versicherungsgedanke und seine historischen Grundlagen* (V&R Unipress, 2011) 281.

[50]Cf Liselotte Eriksson, 'Industrial Life Insurance and the Cost of Dying; The Role of Endowment and Whole Life Insurance in Anglo-Saxon and European Countries during the late Nineteenth and early Twentieth Century' in Robin Pearson (ed), *The Development of International Insurance* (Pickering & Chatto, 2010) 117–32.

'retail insurance products' such as life insurance and burial insurance.[51] Also, the push for solidarity concerning specific social risks such as health, unemployment, and industrial accidents not only resulted in social insurance but also in specific regulated forms of private insurance.[52]

2. *Liability insurance*

Popular understanding is that liability insurance was an invention of the nineteenth century.[53] As one author claims, 'at the beginning of the 19th century, liability insurance would have been unthinkable. It would have been considered as immoral.'[54] This is an appealing narrative. Perhaps the idea of shielding insureds against *the risks of litigation,* indeed, repelled some people as they saw it as an open invitation for the moral hazard of fuelling risk-taking behaviour and inundating courts with unmeritorious claims and undeserving defendants. For this reason, some forms of insurance were perhaps considered to be *contra bonos mores*.[55] An alternative narrative may be that liability risks were 'pure economic risks' – the insurable interests were the assets of the insured as a whole, not – as is the case with building insurance – a specified building at risk from destruction by fire. There is no reason, however, to assume that insurance against 'pure economic risks' was considered less ethical or legally binding than the insurance of tangible

[51] In the nineteenth century, the sale of insurance for children became popular. It aimed at expanding the working-class insurance market and was actively marketed. See, eg, Viviana A Zelizer, *Pricing the Priceless Child – The Changing Social Value of Children* (Princeton University Press, 1985/1994) 115. There were products covering burial costs and fixed sum insurance products (ie, life insurance). Unless the child was the breadwinner, the latter form was irrational to buy. Yet, its popularity was irrefutable (*ibid*, 136). Note that in earlier centuries, annuities were already used to similar ends. See Van Leeuwen (n 38) 92–93.

[52] For instance, in the USA the introduction of employers' liability (workmen's compensation) created demand in the 1880s for a new insurance. See Martin Phelps Cornelius, *Third Party Insurance* (The Insurance Field Inc, 1920) 66. Note that the introduction of compulsory insurance may create a demand which did not exist before. For instance, prior to 1969, when employer's liability insurance was made compulsory in the UK, there was little demand for such a product. Cf Robert Lee Carter and Peter Falush, *The British Insurance Industry Since 1900 – The Era of Transformation* (Palgrave Macmillan, 2009) 93–94.

[53] Schug (n 49) 282. Note that in early literature, liability insurance is sometimes referred to as 'third party insurance'.

[54] André Tunc, *Introduction to the International Encyclopedia of Comparative Law* (Brill, 1974), chapter 1, vol 11, 50, as cited by Patrick M Liedtke, 'The Economic System as Catalyst for Evolving Liability Regimes' (2005) 30 *Geneva Papers on Risk and Insurance – Issues and Practice* 343. In a similar vein for USA law but without cited authority, Kenneth S Abraham, 'The Rise and Fall of Commercial Liability Insurance' (2001) 87 *Virginia Law Review* 86.

[55] A similar narrative could be developed concerning legal expenses insurance as it was sometimes suspected of fuelling litigation rather than stimulating the amicable settlement of disputes, and thus interfering with a balanced operation of the law.

assets at risk. For instance, in marine insurance, it was already held that the creditor of the ship owner – for instance, the creditor under a sea loan or bottomry, that is a loan where the repayment is conditional on the fortunes of the vessel – had an insurable interest in the ship.[56] So the creditor could insure against his pure economic loss which he would incur if the ship perished, effectively using insurance as a credit risk-hedging device. The same 'hedging' occurred as early as the late Middle Ages with annuities for the life of the seller (the debtor): the buyer could insure against the seller's death.[57]

Therefore, no matter how appealing these narratives may sound, there is very little evidence that liability insurance contracts as such were held null and void for any of these reasons. For that reason, I am not convinced that liability insurance was really held to be immoral or *contra bonos mores*. Yet it may well have been considered *alien* as far as terrestrial risks were concerned. That being said, the concept of mutual assistance and support against claims raised by third parties as such was not unfamiliar to guilds. In the Middle Ages, to the extent that commercial risks included liability risks, guild members were potentially liable to indemnify and support their fellow members in litigation.[58] The most plausible reason for the late development of liability insurance can be found, I think, in the lack of demand and the lack of a proper business model for such risk transfers. For instance, when the demand for liability insurance for collision of vessels at sea grew, commercial insurers were reticent to answer with any supply for such risks: they did not have sufficient experience to rate premiums, they feared moral hazard and they lacked the capital, or so they said. The response by ship owners was to help themselves to mutual insurance by means of P&I Clubs ('Protection and indemnity') to cover collision risks.[59] Only later did commercial insurers catch on with (limited) coverage against such liabilities.

So, the fact is, that it was not until early 1900s that general terrestrial liability insurance as a product established itself as a viable business.[60] When it did, there was little doubt that liability insurance was legitimate and legally binding. Policy

[56]Guido Rossi, *Insurance in Elizabethan England – The London Code* (CUP, 2016) 185–91.

[57]*Ibid*, 411–29; Schug (n 49) 243.

[58]Schug (n 49) 152. Yet, the most likely scenario is that they offered mutual support in case of damage to goods and businesses. *Ibid,* 145–46.

[59]Rob Merkin and Jenny Steele, *Insurance and the Law of Obligations* (OUP, 2013) 58, 60.

[60]For the USA, the late 1880s to early 1900s seem to be accurate. Cf Cornelius (n 52) 28; Sachin S Pandya, 'The First Liability Insurance Cartel in America, 1896–1906' (2011) 29 *Law and History Review* 375. Europe followed some time later. Eg, Evan James Macgillivray, *Insurance Law* (Sweet and Maxwell, 1912) 969, spends two pages on the subject and the authorities cited there are all from the USA. That said, specific policies may have been available earlier in some countries. See, eg, Merkin and Steele (n 59) 124, who refer to boiler liability insurance. See also the rise of employers' liability insurance from the 1880s (cf Abraham (n 54) 86–88).

terms included or excluded the costs of litigation and so contracts for insurance against litigation risk for defendants came into existence.[61]

3. *Legal expenses insurance*

Legal expenses insurance as a commercial insurance product developed only in the 1900s;[62] where and when, depended very much on local circumstances. Consider, for instance, countries where the local bar had a tradition of rendering services *pro bono* to the poor. It makes perfect sense to expect LEI not to have developed there as much as it would have done in countries where attorneys were not bound to participate in such systems of solidarity with the poor. The same logic would perhaps apply to countries where state-funded legal aid had developed early on.[63]

Before 1800, guild members were part of a risk community. The guilds offered assistance in legal affairs as well, although this did not really amount to 'legal expenses insurance' in modern terms. What the assistance did probably do, was to offer enough legal help to suffice for the economic purposes of the guild members.[64] Between 1800 and 1900, nothing much happened to fill the void left by the abolition of guilds. To be fair, in many countries there was a culture of *pro bono* lawyering at the bar. This culture of free services for the poor had been around for centuries, voluntarily as part and parcel of the *officium nobile* (and a form of hazing for new members of the bar) or less voluntarily as part of the rulers' cheap way of providing free legal aid.[65] In the late 1800s, legal aid and assistance was viewed less in terms of mercy and charity, and increasingly as an entitlement for the working classes and their families to secure substantive

[61] Cf Merkin and Steele (n 59) 393–94.

[62] Around 1800, isolated attempts to obtain cover for legal expenses (as an ancillary cover with fire insurance) failed. See Pearson (n 42) 293. Insurance companies were simply unwilling to cover such expenses. Around 1900, France took the first steps (*Prévoyance judiciaire* 1885; *Defense Automobile et Sportive* 1917). Switzerland and Germany followed suit (DAS 1926, ARAG 1925). The Benelux followed in the 1960s and Britain in the 1970s; see Georges Hamon, *Histoire Générale de l'Assurance en France et a l'Étranger* (l'Assurance Moderne, 1885) 240–41; Carter and Falush (n 52) 98; Peter Koch, *Geschichte der Versicherungswirtschaft in Deutschland* (VVW, 2012) 244, 372–73.

[63] The reverse is possibly true as well: where the state retreats from funding legal aid, the demand for LEI may grow.

[64] On guild assistance, see, eg, Schug (n 49) 152–64.

[65] See, eg, Donald Robertson, 'Pro Bono as a Professional Legacy' (2001) 19 *Law Context: A Socio-Legal J* 97–127; Emile WA Henssen, *Twee eeuwen advocatuur in Nederland 1798–1998* (Kluwer, 1998) 92. In the Netherlands, for instance, the free advocacy introduced by Napoleon (Imperial Decree 14 Dec 1810) introduced a 'Bureau de consultation gratuite'. The sovereign prince Willem (later King Willem I) decreed in 1814 that the poor and indigent were to have free access to courts (that is nominally speaking, as the practical obstacles were formidable).

equality.[66] With this development 'from alm to entitlement', the balance gradually shifted from *pro bono* work, guilds, trade unions and charitable bodies' assistance to systems of comprehensive state-funded legal aid or private market solutions such as LEI.[67]

When LEI finally got a foothold in twentieth century Europe, it did not experience any of the religious or cultural resistance that earlier financial products such as money lending, insurance and annuities had encountered in earlier centuries. Obviously, there may have been objections against LEI as some may have argued that it would fuel litigation rather than stimulating the amicable settlement of disputes and thus would interfere with a balanced operation of the law. However, it seems that the more serious resistance came from the bar. In most countries, by the second half of the 1800s, members of the bar had properly organized themselves, partly in response to the meagre remuneration standards set by statute, but also by the surge of competition by self-proclaimed quasi-lawyers. For instance, between 1850 and 1900 there was growing dismay concerning unqualified 'quasi-lawyers' ('Winkeladvokaten', 'corner advocates' or pettifoggers) who offered simple advice and assistance in legal matters. At the same time, unions and city councils sometimes offered similar services. Attorneys admitted to the bar felt they had to secure their livelihoods and did so where they could by exercising their political influence. In some countries, the bar successfully lobbied for obtaining monopolies and banning others from the market of legal advice.[68] To this day, in Europe the influence of the bar resonates in the regulation of the markets for legal services. Wherever attorneys are threatened with being replaced by cheaper (and probably less qualified) paralegals, they will resist and use their political power to maintain their position. And they did so in response to LEI, wherever it threatened their business model.[69]

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[66]Robertson (n 65) 98.

[67]For a picture of this development, see, eg, Cornelus JM Schuyt, Kees Groenendijk and Ben Sloot, *De weg naar het recht – een rechtssociologisch onderzoek naar de samenhangen tussen maatschappelijke ongelijkheid en juridische hulpverlening* (Kluwer, 1976) 5; Brian Abel-Smith and Robert Stevens, *Lawyers and the Courts – A Sociological Study of the English Legal System 1750–1965* (Heinemann 1967) 135.

[68]See, eg, the 1883 *Gesetz, betreffend Abänderung der Gewerbeordnung* (1883 Competition Intervention Act), s 35 which created the powers for local authorities to shut down a legal services agency that offered legal advice if its business quality was inadequate ('unzuverlässig'). See generally on the German historical path Hiroki Kawamura, *Die Geschichte der Rechtsberatungshilfe in Deutschland (diss Berlin)* (BWV, 2014) 133–37, 178–212, 241–74. See for a similar problem in England, Abel-Smith and Stevens (n 67) 138, who point to a surge in commission agencies in the late 1800s, causing a 'black market in legal aid' where aggressive claims management agencies attracted business as a speculation in claims. Generally, on the 'politics of the profession' Richard L Abel, *English Lawyers between Market and State: The Politics of Professionalism* (Oxford socio-legal studies, OUP 2003) 471.

[69]For instance, we can see this in art 201 Directive 2009/138/EC on the taking up and pursuit of the business of Insurance and Reinsurance (Solvency II) (formerly: Legal Expenses Insurance Directive 87/344/EEC; now repealed) and how it has been used in

IV. Investing in potential litigation gains

1. *Investment generally*

When looking at the historical development of the legal discourse surrounding investment in litigated claims, a distinction may be made between attorney investment and third-party investment. Concerning attorney investment in litigation gains, throughout history we can observe a strong view that attorneys should not invest in their client's claim. It was often felt that such investment would be much like allowing attorneys to wager on their own cases; it was thought that it could cloud their judgment by substituting the inner motives of the *officium nobile* with a worldly lust for money (in other words: *wagering*), and that it could lead them to stipulate excessive shares in the proceeds to clients under financial duress (in other words: *usurious contracts*). In third-party investment in potential litigation gains, the narrative developed slightly differently, although the objections against usury also played a significant part. Essentially, the main objection was a fear of abuse of the court system for commercial gain or abuse against public interests. Third-party investors in claims were somehow suspected of stirring up litigation and thus interfering with the fair and just operation of the legal machinery (in other words: *champerty and maintenance*). This section explores these objections to attorney investment and third-party investment.

2. *Attorney investment in their client's claim*

As with much legal discourse, any legal discussion about the validity of contracts for the transfer of litigation risk starts with the question: *what did the Romans think?* If the Romans did not like such contracts, the chances are that the influence of Roman law can be witnessed through the Middle Ages, well up to and perhaps even beyond the Age of Enlightenment.[70] And that is exactly what we find when it comes to claims investment by attorneys. The short story is that the Romans were not keen on contracts for the transfer of litigation risk, especially not when lawyers as a result gained more than a modest fee.[71] But lawyers cannot live on air alone; they have to make a living and therefore somehow need to charge fees for their services.[72] The 'advocatus' who helped litigating parties, became a privileged

recent years to obstruct the 'in kind' business model of some LEI insurers. Cf Merkin and Steele (n 59) 387.

[70]Rossi (n 9) 324.

[71]See Ulp D 2.14.53; Ulp D 50.13.1.12; C 2.6.5; C 2.6.6.2.

[72]The names and forms under which attorneys charge, differ over time and jurisdiction. Sometimes, we find the Latin phrases *salarium*, *honorarium* and *palmarium*. The first, *salarium*, mostly denotes a fee for a service, an *honorarium* can be either a fee for services or a retainer *strictu sensu*, that is a fee for promising future services, and a *palmarium*, a bonus out of gratitude if the case is dealt with satisfactorily. See Brundage (n 1) 8. The bonus was gratuitous and any pre-trial promise to pay a bonus was deemed unenforceable according to Johann F Autenrith, *Dissertationem Inauguralem Iuridicam De Eo Quod Iustum Est Circa*

class subject to state supervision and licensing. With this development, a change of attitude also occurred in relation to the compensation for services rendered. The honour to serve developed into an *honorarium*, the amount of which was left to the parties to negotiate, but at the same time there was some sort of cap. Usually, it remained unlawful to enter into a contingent fee *pactum de palmario* (a fee or bonus contingent on success) or a *pactum de quota litis* (a percentage of the claim conditional on success).[73] We already find this sentiment in Roman law.[74] From then onwards, it seems to percolate right through to early medieval authority and early modern jurisdictions.[75] For example, Kames (1778) writes:

> A pactum de quota litis is in itself innocent, and may be beneficial to the client as well as to the advocate: but to remove the temptation that advocates are under to take advantage of their clients instead of serving them faithfully, this court declares against such actions.[76]

To this day, this sentiment – intuitive, however, rather than evidence-based[77] – remains at the basis of the virulent dislike of such *pacta* in many countries on

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Salaria Ac Honoraria Advocatorum (Von den Advocaten-Gebühren) (diss) (Wittenberg 1727) 23.

[73] Arthur Engelmann, *A History of Continental Civil Procedure* (The Continental Legal History Series, Little, Brown and Company 1927) 342.

[74] See, eg, Reinhard Zimmermann, *The Law of Obligations* (Clarendon, 1996) 415, 12–714; Brundage (n 1) 1–15; Gergely Deli, *Salus rei publicae als Entscheidungsgrundlage des römischen Privatrechts* (Medium, 2015) 9.

[75] Eg, Brundage (n 1) 1–15; Carol R Andrews, 'Standards of Conduct for Lawyers: An 800-Year Evolution' (2004) 57 *SMU L Rev* 1385, 1393, 1411; Hannes Siegrist, *Advokat, Bürger und Staat – Sozialgeschichte der Rechtsanwälte in Deutschland, Italien und der Schweiz (18.-20. Jh.) – Erster Halbband* (Vittorio Klostermann, 1996) 254.

[76] Henry H Kames, *Principles of Equity (2014 ed. by M Lobban, Librty Fund Inc)* (Bell, Creech & Cadell, 3rd edn 1778) Vol I, 17. James, Viscount of Stair, *The Institutions of the Law of Scotland* (1681), I 10.8 already stated that a *pactum de quota litis* whereby advocates or agents take a share of the profit of the pleas is rejected 'both by the civil law and our custom, whether it be a naked promise or mutual contract'. Such *pacta* were 'reprobated by the civil law and by the custom of all nations' (*Ruthven v Weir* (1680) Mor 9499 at 9499, as quoted by Laura J Macgregor, 'Pacta Illicita' in Kenneth Reid and Reinhard Zimmerman (eds), *A History of Private Law in Scotland – II. Obligations* (OUP, 2000) 139).

[77] On the behavioural aspects of lawyer remuneration, see, with further references, Willem H Van Boom, 'Financing Civil Litigation by the European Insurance Industry' in Mark Tuil and Louis Visscher (eds), *New Trends In Financing Civil Litigation In Europe – A Legal, Empirical, and Economic Analysis* (Edward Elgar, 2010) 92–108; Willem H Van Boom, 'Juxtaposing BTE and ATE – On the Role of the European Insurance Industry in Funding Civil Litigation' (2010) *Oxford U Comparative L Forum* (ouclf.iuscomp.org); Willem H van Boom, *Third-Party Financing in International Investment Arbitration (Report for the OECD)*, 2011, at https://doi.org/10.2139/ssrn.2027114; Willem H Van Boom (ed), *Litigation, Costs, Funding and Behaviour – Implications for the Law* (Routledge, 2017).

the European continent and the British Isles.[78] In England, the doctrines against 'maintenance and champerty' (see further below) constituted a firm bulwark against conditional fees. The legal profession also frowned upon the idea of a lawyer having a financial stake in a case.[79] After World War II, the English relied on 'the most radical scheme of socialized legal services in the West'.[80]

However, given that the issue was, and still is, discussed so frequently in legal writing, such contracts must in fact have occurred and continue to occur in legal practice.[81] The reason for this may be the utter greed of lawyers, but alternative motives also play a role: if clients cannot pay in advance for the legal services, there may be a good reason to negotiate a conditional fee. Impecunious clients may actually want such contracts if there is no proper state-funded legal aid or pro bono system in operation.[82] Interestingly, where Europe continued to dismiss conditional fees, *pacta de quota litis* in particular, the USA changed track in 1800s as the 'American rule' for cost shifting in civil proceedings emerged. This was not a coincidence. There was a growing feeling that attorneys and their clients should be free to enter into any fee arrangement they wanted, since it was the client who had to pay for his own legal costs, win or lose.[83] This may point to a relationship with cost-shifting rules and the dislike of *pacta de quota pars litis*.

3. *Third-party investment*

In the previous section, we looked at the sentiments relating to attorney fees. The picture that emerged is that, over the centuries, attorneys were allowed to charge fees, usually an *honorarium*, a fee based on the number of hours worked on the case, or perhaps even a fee mark-up if the case was won (eg, a *palmarium*). Sometimes, fees were regulated and capped. In any event, a full-fledged *pactum de quota pars litis* was, and mostly still is, unacceptable to most legal systems (the USA being an exception). Understandably, third parties have tried to step in and provide such a *pactum* to claimants who felt the need for it, when and where such products were legally admissible and enforceable. To understand how

[78]In fact, the recent discussions on facilitating mass litigation in Europe are also founded on this exact dislike. See Ilja Tillema, *Entrepreneurial Mass Litigation; Balancing the Building Blocks (diss Rotterdam)* (https://repub.eur.nl/pub/114523) (2019).

[79]In 1910, the Rule Committee of the High Court more or less suggested allowing contingency fee arrangements, but the Bar Council was quick to criticize this plan as a strong inducement for speculative actions. Abel-Smith and Stevens (n 67) 140.

[80]*Ibid,* 315. Note that in Scotland, the idea of supply of legal aid on a 'no cure no pay' basis was met with less hostility. *Ibid*, 319.

[81]Brundage (n 1) 9.

[82]Moreover, in many instances, lawyers' fees were regulated by the state, but because such regulations often remained unchanged for long periods there was a reason for ignoring and circumventing such regulations. Brundage (n 1) 12–15.

[83]John Leubsdorf, 'Toward a History of the American Rule on Attorney Fee Recovery' (1984) 47 *Law & Cont Problems* 9, 9–36.

legal systems have shaped their responses in the last few decades, we need to briefly revisit the historical context of doctrines such as maintenance and champerty, and the issue of the legality of assignment of claims.

a. *Maintenance and champerty*

In medieval times, the available dispute resolution mechanisms in England had a potential for misuse and corruption. They could fall prey to conspiracy, barratry, maintenance, and champerty.[84] *Conspiracy* took the form of false indictments, *barratry* was the bringing of vexatious litigation, *maintenance* was intermeddling in litigation by providing assistance or support to a party in proceedings in which the maintainer was not a party.[85] It was the 'assistance in prosecuting or defending a lawsuit given to a litigant by someone who has no bona fide interest in the case [or] meddling in someone else's litigation'.[86] *Champerty* referred to stirring up a lawsuit; this was a form of maintenance, where the maintainer without any pre-existing legitimate interest in the outcome of the action was promised all or part of the proceeds or the disputed subject matter in exchange for the assistance.[87] Several statutes were passed to curtail what were considered to be disturbing misuses.[88]

Although it is debatable whether the medieval statutes prohibiting maintenance actually had any effect (in fact, they may have been abused to bring maintenance actions to harass adversaries),[89] they have haunted the legal debate in

[84]In medieval times, most civil litigation involved land and ownership. Such litigation was in part about power and hierarchy and thus had an impact on public order, which perhaps explains why those in power were nervous about maintenance and champerty. With the Industrial Revolution, the nature of civil cases started to change. From the 1800s, commercial exchange, accidents, labour disputes, tenancy, and consumer issues became more important than before. See Abel-Smith and Stevens (n 67) 136–137.
[85]Blackstone (n 17) IV 135. Cf *Unruh v Seeberger* [2007] 10 HKCFAR 31 (per Mr Justice Ribeiro PJ) at 82–88.
[86]Black's Law Dictionary.
[87]Jonathan Rose, *Maintenance in Medieval England* (CUP, 2017) 346; Peter C Choharis, 'A Comprehensive Market Strategy for Tort Reform' (1995) 12 *Yale Journal on Regulation* 435, 460–525.
[88]For an overview of the historical development of these principles, eg, Percy H Winfield, 'The History of Maintenance and Champerty' (1919) 35 *Law Quarterly Review* 50, 50–72; Choharis (n 87) 460; Vicki Waye, *Trading in Legal Claims* (Presidian Legal Publications 2008) 12; Maya Steinitz, 'Whose Claim Is It Anyway? Third-Party Litigation Funding' (2011) 95 *Minnesota Law Rev* 1286–1338; Charles Silver, 'Litigation Funding versus Liability Insurance: What's the Difference?' (2014) 63 *DePaul Law Review* 617, 631–1093; David S Abrams and Daniel L Chen, 'A Market for Justice: A First Empirical Look at Third Party Litigation Funding' (2013) 15 *University of Pennsylvania Journal of Business Law* 1075, 1082–1111; David Neuberger, *From Barretry, Maintenance and Champerty to Litigation Funding (Harbour Litigation Funding First Annual Lecture; Grey's Inn, 8 May 2013)* (2013) 5–25.
[89]Rose (n 87) 9.

common law jurisdictions up to this day. For instance, in the seventeenth and eighteenth century, the view developed that *not all* assistance was unlawful. However, a good method to distinguish permissible forms from the prohibited practices was not available,[90] rendering this area of the law highly unpredictable. Also, in the sixteenth century, the emergence of solicitors – unqualified lawyers, next to barristers and attorneys – was initially curtailed by the maintenance doctrine itself. Eventually, solicitors became an established type of lawyers.[91]

After World War II, a distinct difference between English law and the legal position of the USA came to the fore. Although in the USA the doctrines of maintenance and champerty had had a mixed reception (some states have banned the common law doctrines, others have embraced them and again others have restricted their scope),[92] the idea of *attorneys* being retained on the basis of a *quota pars litis contingency fee* became accepted.[93] Meanwhile, the idea was rejected in England.[94] Although a 1966 Law Commission report advised in favour of abolition of the medieval doctrines against maintenance and champerty,[95] the Criminal Law Act 1967 which ensued, decriminalized champerty and maintenance by repealing many of the medieval statutes and abolished tortious liability for maintenance and champerty. However, the civil remedy in contract (unenforceability of contracts for maintenance or champerty) remained.[96]

In contemporary English law, the prohibition of champerty and maintenance is chaotic and unprincipled. Although it is sometimes stated that it is plain 'that the application of the old law of maintenance and champerty is attenuating not increasing,'[97] the state of affairs under English law remains unsettled. If a contract contravenes the prohibition of maintenance and champerty, it is considered invalid.[98] To this day, this hangs like a dark cloud over any transaction involving investment in a litigated claim. For instance, a contingency fee agreement between a client and an accountant was deemed lawful, as was a conditional fee agreement between a client and a solicitor under which the solicitor agreed to indemnify the

[90] *Ibid*.
[91] *Ibid*, 356.
[92] Waye (n 88) 111.
[93] Max Radin, 'Maintenance by Champerty' (1935) 24 *California Law Review* 70.
[94] *In re a Solicitor* [1912] 1 KB 302; Law Commission, *Proposals for Reform of the Law Relating to Maintenance and Champerty* (HMSO, 1966) 6; cf Alfred D Youngwood, 'The Contingent Fee – A Reasonable Alternative?' (1965) 28 *The Modern Law Review* 330, 331.
[95] Law Commission (n 94) 3–36.
[96] S 13 and S 14 Criminal Act 1967. See Marcus Smith, *The Law of Assignment: The Creation and Transfer of Choses in Action* (OUP, 2007) 318; Rose (n 87) 359.
[97] *Murray Lewis v Tennants Distribution Ltd.* [2010] EWHC 90161 (Costs) at 18 (O'Hare, costs judge).
[98] Nicholas Rowles-Davies and Jeremy Cousins, *Third Party Litigation Funding* (OUP, 2014) 22. Cf Michael Zander, 'Will the Revolution in the Funding of Civil Litigation in England Eventually Lead to Contingency Fees' (2003) 52 *DePaul Law Review* 259, 260.

client against adverse cost orders.[99] However, as recently as 2011 the Court of Appeal held that the assignment of a cause of action for the purposes of enabling the assignee or a third party to make a profit out of the litigation will generally be considered void as savouring of champerty.[100]

Moreover, the 1990s saw a drastic overhaul of civil procedure funding. State-funded legal aid was more or less abolished and in its place, the so-called Woolf Reforms introduced a specific contract for the transfer of litigation risk, the conditional fee arrangement (CFA).[101] This basically allowed lawyers to agree to a success fee.[102] However, the CFA together with English cost rules and a mushrooming of insurance funders turned out to be a 'toxic mix'. The 2013 Jackson Reform which resulted from this, starved most of the CFA arrangements of their fuel.[103] The alternative Damages Based Agreements (DBAs) it introduced have yet to show their potential. So, in summary, England and Wales have seen a 'rise and fall' of certain contracts for litigation risk transfer, but the remainder have in any case moved away from the minefields of maintenance and champerty – not only as far as the position of attorneys is concerned, but also in relation to third-party litigation funding. In England and Wales, third-party litigation funding is allowed, be it with certain restrictions, as it is thought to increase access to justice. This echoes the position in the early 1900s.[104]

b. *Assignment and other hiccups*

Problems with assignments and doctrines such as 'retrait litigieux' are relevant to third parties who would like to enter into a *pactum* to invest in a claim. The risk of investing in the proceedings is transferred by means of the *pactum* in return for a *pretium periculi*, a share in the proceeds when the claim is successful. In a sense, by agreeing to such a conditional price and thus classifying the contract as an aleatory contract instead of a money loan with an excessively high interest rate, any ethical concerns stemming from a historically rooted dislike of usury in the strict sense can be avoided. For this *pactum* to work, the investor will want to

[99] *R (Factortame) v Secretary of State for Transport, Local Government and the Regions (No. 8)* [2003] QB 381; Sibthorpe v London Borough of Southwark [2011] EWC Civ 25.
[100] *Simpson v Norfolk & Norwich University Hospital NHS Trust* [2011] EWCA Civ 1149 at 15 (per Moore-Bick LJ).
[101] Courts and Legal Services Act 1990.
[102] See for an overview of the development in England and Wales until the 2013 Jackson Reform, eg, Waye (n 88) 83; Zander (n 98) 260–98. Much like a contingency fee, the CFA retainer operated on the result obtained on behalf of the claimant. Cf *ibid,* 294.
[103] Rupert Jackson, *Review of Civil Litigation Costs – Preliminary Report* (London, 2009); Rupert Jackson, *Review of Civil Litigation Costs – Final Report* (London, 2010); Ministry of Justice, *Reforming Civil Litigation Funding and Costs in England and Wales – Implementation of Lord Justice Jackson's Recommendations – The Government Response* (Ministry of Justice, 2011), on which Merkin and Steele (n 59) 382–406.
[104] See Edmond Bodkin, *The Law of Maintenance and Champerty* (Stevens and Sons, 1935) 6; Rose (n 87) 364.

have as much control as possible over the claim itself and the conduct of the proceedings. Ideally, assignment of the claim itself could have this effect; the defendant would not be notified of the assignment and the original claimant would formally conduct the litigation. This is problematic for several reasons. One of the reasons lies in the historical roots of the law of assignment. For instance, in common law jurisdictions the assignability and survivability of claims is not one coherent doctrine. Originally, the common law more or less prohibited the assignment of choses in action at law; equitable exceptions existed.[105] This position has been relaxed somewhat, but certain assignments have remained unenforceable champerty.[106] Sometimes the distinction is made between assignment of a *cause of action* and an assignment of the *fruits* of a claim, where the latter is more straightforward (judgments constitute property) than the former.[107] On the contrary, things are not necessarily more straightforward. Although in some continental legal systems the assignment of claims for the purpose of debt collection transfer of title or security is unproblematic, this is not a unanimous position.[108] In short, assignment of the claim is not always readily available as such. Furthermore, assignment to a third-party investor may run into trouble for other reasons. For instance, in France, the assignment may also provoke the 'retrait litigieux' doctrine.[109] This doctrine entails that when a contested claim is brought before a court and subsequently assigned pending proceedings, the debtor can release the debt by paying an amount equal to the price paid for the claim by the assignee (art 1699 Code Civil). The doctrine seems to serve as a disincentive against speculating on ongoing proceedings.[110] However, the article does not cover assignment concluded *before* the start of proceedings, so its scope is rather haphazard.

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[105] Smith (n 96) 128; Greg Tolhurst, *The Assignment of Contractual Rights* (Hart Publishing, 2006) 11–28.

[106] Rose (n 87) 360; Waye (n 88) 120–21; Tolhurst (n 105) 121–321. In *Trendtex Trading Corp v Crédit Suisse* [1982] AC 679 (HL), the House of Lords introduced a test of genuine commercial interest. If the assignee has a genuine commercial interest in enforcing the claim for their own benefit, the assignment is valid. Following the *Trendtex* test, it has been argued that, in principle, the proper and genuine assignment of debt, (other) contractual causes of action, most tortious causes involving pure economic loss, and restitutionary causes are valid. Smith (n 96) 321. Cf also the 2009 High Court decision in *Rawnsley and the Canal Dyeing Cy Ltd (in liquidation) v Weatherall Green & Smith North Ltd and O'Hara (liquidator)* [2009] EWHC 2482 (Ch) at 73. In *Rawnsley*, the High Court held that an outright assignment of a cause of action by a liquidator for monetary consideration of 10 percent of the net proceeds is valid.

[107] On the procedural requirements for assignment in S 136 Law of Property Act 1925, see *Torkington v Magee* [1902] 2 KB 427.

[108] See, eg, Tillema (n 78); Van Boom (n 1) 5–30.

[109] Generally speaking, French law does not seem to be receptive to arrangements involving speculation with claims. See François Terré, Philippe Simler and Yves Lequette, *Droit civil – Les obligations* (Dalloz, 10th edn 2009) 1283–84.

[110] Andrea Pinna, 'Financing Civil Litigation: The Case for the Assignment and Securitization of Liability Claims' in Mark Tuil and Louis Visscher (eds), *New Trends in Financing*

V. Discussion and conclusion

In the previous sections, I reviewed contracts for litigation risk transfer, insurance against litigation risk and contracts for investment in litigation gains. One of the emerging patterns is a difference in narrative between insurance and investment concerning litigation risk: although both share an identical economic rationale, they have been treated differently by the law over the ages.

Ancient legal obstacles such as usury and a dislike of contracts involving risk transfer (see Section II) may have hampered the development of 'terrestrial insurance' in earlier centuries and this, in turn, may have provided a narrative against bringing liability insurance and legal expenses insurance to the nineteenth and twentieth century markets. On balance, however, my impression is that this narrative is misleading (see Section III). It seems that if insurance companies were not keen on providing this type of insurance at first, it was not because they thought it was going against good morals or public policy but because they did not have any experience with pricing such a product. More decisive for the growth of demand for these contracts were the environments in which they had to manifest themselves; there, factors such as alternative sources for legal aid (guilds, state-funded legal aid, pro bono lawyering) come into play.

Contrastingly, the narrative of 'good morals or public policy' seems to be stronger when it comes to attorney investment and third-party investment (see Section IV). What we consistently find in European legal systems, is that of a strong opinion against attorneys investing in their own client's claim. For some reason, it was – and still is – felt by many that such an investment is unethical. The reasoning is strikingly similar to the objections that have been raised over the centuries against certain other contracts. Sometimes, it is said that attorneys should not be allowed to invest in their own claims portfolio because it clouds their judgment by substituting the inner motives of the *officium nobile* with a worldly lust for money. That is the wagering narrative. In turn, this may lead them to extract excessive benefits by stipulating ludicrous shares in the proceeds to clients under financial duress. This is the usury narrative. Also, we find opinions to the effect that third-party investors in claims only stir up litigation and thus interfere with the fair and just operation of the legal machinery. This is the champerty and maintenance narrative.[111]

Such narratives have firm historical roots and perhaps that is why they appeal from a rhetorical point of view. It does not mean, however, that they are factually correct.

Civil Litigation In Europe – A Legal, Empirical, and Economic Analysis (Edward Elgar, 2010) 116.

[111] Cf Victoria Shannon, 'Harmonizing Third-Party Litigation Funding Regulation' (2015) 36 *Cardozo Law Review* 861–912.

Acknowledgements

Earlier versions of this paper were presented at the 2019 British Legal History Conference, St Andrews, Scotland, and at the 2019 International Conference on Risk and the Insurance Business in History, University of Sevilla, Spain.

Disclosure statement

No potential conflict of interest was reported by the author(s).

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