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SEVEN STARS LEGAL FUNDING LIMITED

SECURITY FRAMEWORK PAPER

Seven Stars Legal – Security Framework

Introduction

This paper outlines the “Security Framework” implemented by Seven Stars Legal Limited to protect investor capital and ensure the delivery of stable returns to investors.

Background

The United Kingdom’s legal sector is one of the most well-regarded in the world.

A May 2024 report published by the Legal Services Board, led by Professor Rachael Mulheron KC (Hon), Professor of Tort Law and Civil Justice at Queen Mary University of London and one of the country’s leading legal academics, highlighted the vital role that litigation finance has to play in both facilitating access to justice but also helping the country’s legal sector maintain its global standing and reputation.

While this report, and most of the UK’s growing litigation finance sector, predominantly focuses on large-scale collective actions – known as class actions in the United States but, until recently, rarely seen in the UK – at Seven Stars, we operate at the opposite end of the sector, focusing on smaller, precedent-based case types with lower, fixed costs that allow us to achieve an attractive rate of returns for our investors while minimising the risk involved.

This paper examines our approach to litigation finance, how we diversify and mitigate risk.

Seven Stars Legal – What We Do

Seven Stars operates exclusively within established regulatory frameworks in the UK, providing funding to SRA-regulated law firms and FCA-regulated claims management companies enabling “no win, no fee” representation for individual claimants who cannot afford legal costs.

We seek to capitalise on a diversified portfolio of vetted legal cases, where the potential for favourable outcomes presents an exciting prospect for investors seeking what is a primarily uncorrelated asset. We achieve this by focusing on process-orientated claims with proven track records or clear mandates from the Superior Courts or Governmental schemes.

Funds are lent at a set annual interest rate that is competitive for the sector and may also benefit from a preset share of the Solicitor’s income as an additional profit element.

Track Record

Seven Stars Legal has established a proven UK litigation funding platform, which has successfully deployed funding across 40,000+ cases with a 36% average ROI.

Our team has extensive experience in litigation funding with over 100 years collective professional expertise in private credit, fund management and litigation funding sectors, having managed in excess of £1 billion of claim values in the past decade.

Management team: 100+ years collective professional experience

Track Record: £1 billion+ in funded claim values managed

Current security ratios: the end of Q4, we sit at a security ratio of 2.30:1 against capital lent, and at 1.73:1 against our overall contract debt.

Proprietary Capital Preservation Reserve: 20% settlement escrow

Real-time case monitoring: Independent third-party auditing via Insyte IQ

Partnership base: Diversified relationships across 9+ SRA-regulated law firms

Scalable pipeline: Established infrastructure for continued portfolio growth



RISK MANAGEMENT FRAMEWORK

We adopt a layered, disciplined approach building in risk management, embedding protocols at every stage of our lending process:

- **Senior secured position** in all borrower assets with minimum 1.5x coverage
- **Professional indemnity insurance** on all law firm borrowers
- **After the event (ATE) insurance** cover for legal claims
- **Geographic and temporal diversification** across more than 140,000+ individual claims
- **Fixed and floating charge registration** providing strong, enforceable security over borrower assets

What we fund & Why

Seven Stars Legal invests exclusively in the UK and lending to **SRA-regulated law firms** and **FCA-regulated claims management companies** operating within one of the world's most respected and stable legal jurisdictions. We maintain **strict borrower controls** to ensure transparency, compliance, and accountability throughout the funding process.

We specifically target **precedent-based legal claims** or claims under **Government compensation schemes** or **Acts for investment**, which reduces the risks involved. This is because a precedent-based case has already won a court victory and all cases involving the same facts fall under the same judgment.

All funded cases are required to have **After the Event (ATE) insurance** where the case may be settled in the Courts of England or Wales or where a risk of adverse costs may exist.

We will only fund cases against liquid entities, such as Banks and Housing Authorities, or Government compensation schemes such as the FSCS.

In addition to precedent-based legal claims, we also fund Housing Disrepair claims against local housing authorities, mis-sold pension claims made via the FOS/ FSCS, Bank Fraud, Car Finance Mis-selling (PCP) and Contentious Probate claims, and cost advance funding.

By diversifying across a range of small claims, we **mitigate the impact of individual case losses** and ensure **steady capital deployment and recovery cycles**.

Targeting smaller cases enables us to:

- **Maintain tighter cost controls:** we typically establish fixed, specific funding levels for each case type we fund.
- **Minimise risk exposure:** as cases we fund are predominantly precedent based.
- **Deliver consistent returns:** Predictable, steady flow of returns to our investors.
- **Work selectively with regulated law firms:** Law firms with existing cases where we've established it is viable for the firm in question to repay the funding and satisfactorily deliver its services to its client, who in such cases is the claimant.

RISKS & RISK MITIGATION

While our approach to targeting smaller case types is lower risk than funding high-value collective actions, there are still some risks associated with litigation funding. **Our comprehensive due diligence processes** and **lending methodology** minimise the risks to Seven Stars and its investors.

Establishing Minimum Claim Values

When looking at claims a key factor in our investment underwriting process is to establish **minimum claim values** for each sector to ensure sufficient capital cover.

We examine the expected damages in a case to see that there is scope for a healthy return on investment (ROI). Seven Stars lends money to law firms in return for an annualised interest rate, which when coupled with our percentage of the 'No Win No Fee' income, is projected to be sufficient to ensure all parties are paid out in full. This assessment is fundamental to our risk management framework and is used from the outset to evaluate affordability of funding.

Losing a Claim

The entire basis of litigation finance is that a legal case is an asset that can drive a return. As such, a legal case can only deliver a return if it is won and the law firm repays us per the terms of their funding agreement. Our primary means of mitigation against the risk of losing a claim is our comprehensive due diligence processes, which analyse our existing and prospective borrowing law firms and specific case types.

At a case level, our due diligence processes review numerous factors, including existing precedents from Superior Courts or with reference to Government schemes, to understand and ascertain the likelihood of success and for a particular case type to be a profitable funding opportunity.

In respect of the law firms themselves, in addition to the due diligence we conduct when accepting them for borrowing, we further assess each funding request, including a review of the case files for the claims to be funded. As we only fund existing claims, this enables us to ensure that we only fund cases that we believe to be meritorious and are likely to succeed. Underpinning our due diligence processes, we also place several conditions on our borrowing law firms, including an insistence on them having After-the-Event (ATE) insurance, if required.

After The Event insurance

ATE insurance must be in place for all cases funded by Seven Stars where a risk of costs or adverse costs exists. ATE policies cover the cost of 'own disbursements' (the funds spent on that case) on funded cases in the event that a case is lost; in this scenario, it also covers the other party's costs.

It is not a capital insurance for the investment, and Seven Stars is not a beneficiary; however, it does provide assurance that the borrowing law firm will receive funds it can use to cover indebtedness. Each borrower is subject to **active case monitoring**, ensuring transparency over claim progress. Borrowers must either repay or replace funded cases with Seven Stars' consent.

Seven Stars also reserves the right to request that Funding Partners have **rated paper underwriting**, such as an A-rated underwritten ATE policy. If this is required, Kevin Prior, Seven Stars' Chief Commercial Officer, will request and discuss it with the Funding Partner and agreements are written such that this is easily applied as a condition of lending. Equally, lending agreements are not an obligation to fund, and Seven Stars retains the right to cease a funding line should they believe they have reason to do so.

How we mitigate debt security risk

Our lending is **full recourse lending** and Seven Stars Legal takes a charge over the assets of all Funding Partners and the cases being funded. The Funding Partners are charged an interest rate, arrangement fee and sometimes a contractual share of their success fees for winning the cases.

Typically, the potential gains from a successful case must be at **least twice the amount** spent pursuing the case. Losing a case results in usually losing only the sums invested in pursuing the case, most of which can be covered by After The Event (ATE) insurance.

This difference between the potential gains and the potential losses (covered by ATE insurance) provides an element of security and capital protection.

The Funding Partner enters into either a **Deed of Assignment** of funded assets or a **general Debenture** with the lender. The assignment covers all no-win, no-fee (i.e. not profit costs) income due to the Funding Partner, both disbursements and the contingency fee, so it will generally be of greater value than borrowings. Seven Stars aims to provide a minimum level of debt cover of 1.5 times the borrowed amount. In practice, it is closer to twice the borrowed amount on most cases funded but can go as high as four times on Financial Ombudsman Service (FOS) or Financial Services Compensation Scheme (FSCS) claims as a result of our lending evaluation process on these case types.

In the event of solicitor default, Seven Stars holds the **right to reassign** the cases to another firm.

Law Firm Risk

We lend to **regulated law firms or regulated marketing companies**, helping such firms acquire cases while ensuring there is a strict mechanism of controls in place for borrowers. Our Advisory Panel of Legal, Corporate Finance, and Business experts carry out significant due diligence on the financial stability of the law firm and the viability of the cases seeking funding.

If approved by our **advisory panel**, we complete a deed of assignment over the cases and take a debenture over the law firm's assets. In the event of fraud by a legal firm, we could make a claim under the Solicitors Regulation Authority (SRA) Indemnity Fund or the mandated Professional Indemnity (PI) insurance of each Solicitor, which they are obliged to hold.

Diversification

Complementing these safeguards, Seven Stars applies a **self-imposed diversification framework**, known as the **30/30 Rule**, ensuring prudent capital allocation. The 30/30 rule is a straightforward diversification methodology stating that at any given time, we will have a maximum of **30% of all deployed funds** committed to a single law firm or a specific case type.

While we are committed to the 30/30 rule as a long-term foundation for good practice and sound governance, there are occasions when it may be in the best commercial interests of Seven Stars and its investors for our deployed funds in a specific law firm or case type to exceed 30%.

Exceptions to the 30/30 Rule – Solicitors Regulation Authority Fee Cap Impact

In July 2024, the Solicitors Regulation Authority introduced a fee cap for law firms working on financial mis-selling cases in line with the Financial Conduct Authority fee cap for claims management companies. This fee cap changed how we fund certain case types and could significantly impact the profitability of law firms and their capability to use litigation financing to run specific case types. With this in mind, we decided to extend our lending in the pensions mis-selling space before the introduction

of the Solicitors Regulation Authority fee cap so that we could maximise returns before making adjustments to our lending methodology for funding requests received after 26th July 2024, when the fee cap came into force.

This resulted in our case type distribution at the end of Q2 2024 having 34% of our agreed lending committed to pensions mis-selling claims, which our borrowing law firms pursue via the Financial Ombudsman Service and/or the Financial Services Compensation Scheme.

Exceptions to the 30/30 Rule - 2024 Portfolio Rebalancing Exercise

Subsequent signing of new funding agreements and rebalancing activity throughout the second half of 2024, we took a strategic decision to allow our committed funds for housing disrepair claims to exceed 30% given the scale of opportunity in this sector.

With recent developments within the PCP car finance sector in particular the recent high court decision in the Johnson case and the clarifications by the FCA of the redress scheme there is a significant funding opportunity in a sector where clear guidelines are now in place which have derisked the process.

As the 30/30 methodology is a self-imposed rule, while there are some challenges and potential scenarios we must be mindful of within our operations, most of these require us to make decisions in the best interests of our business and investors rather than providing any threat to our viability, and we retain the ability to remain flexible in our approach so we can achieve our objectives.



UNDERWRITING PROCESS

Seven Stars has established a **team of advisors** to oversee the funding requests received from law firms and an established lending **due diligence process** prior to lending, during funding requests, and at regular intervals throughout the loan period. In addition to the internal team, we also engage with external experts (Insyte IQ) to provide further data analysis and due diligence oversight.

The lending lifecycle

1. Approach and interview

Following an initial approach and expression of interest in receiving funding, an interview is conducted with the directors of the prospective Funding Partner by Kevin Prior, Seven Stars' Chief Commercial Officer, and Steve Matthewman of the onboarding team, to understand the company's funding needs, history, and current business position. File notes are taken and retained.

2. Due diligence procedures

Subject to completion of a satisfactory interview indicating the suitability of the Law Firm or regulated marketing company and the cases they run being eligible to receive funding, due diligence procedures are conducted by Steve Matthewman, Seven Stars' Commercial Assistant.

At this stage, Seven Stars sends the prospective Funding Partner a **comprehensive Due Diligence Questionnaire and Checklist** for completion. Upon receipt of this and additional data, Seven Stars compiles a Data Room to hold the information gathered from the prospective Funding Partner, which includes but is not limited to:

- The prospective Funding Partner's policies and procedures, including data protection, disaster recovery and general IT.
- Copies of all template Client retainer documents.
- Relevant insurance policies, including After The Event (ATE) Insurance, if applicable to the case types the prospective Funding Partner is looking to fund.
- Cash flow projections and analysis, to ensure capacity to repay.
- Assessment of case acceptance procedures.
- Review of last filed accounts.
- SRA verification of the Solicitor and firm.
- Complete identification, anti-money laundering, and credit checks on the prospective Funding Partner's company directors.

This ensures each Funding Partner is assessed for **operational integrity, compliance robustness, and repayment capability** before any capital is committed.

3. Initial review and request for funding proposal

Upon satisfactory completion and outcomes of the Due Diligence Questionnaire and Checklist and the relevant checks on the prospective Funding Partner and its company directors, Seven Stars Director Andrew Neal reviews all the gathered information both internal and external.

Once verified and that all necessary information, data are present and acceptable, Seven Stars requests prospective Funding Partners complete a Funding Proposal document.

To ensure consistency in each Funding Proposal, Seven Stars provides its own Funding Proposal document template to prospective Funding Partners and instructions on the information required.

4. Final review and file note

Upon receipt of a completed Funding Proposal, Andrew Neal conducts a further review, checking that the file is complete while also deciding whether Seven Stars wishes to proceed.

If the Funding Proposal is for a case type not previously funded, Seven Stars will also seek **independent opinions** from third-party solicitors about the viability and prospects of success for the case type in question.

If Seven Stars wishes to proceed, a file note containing all the documents, data, and information gathered during the Due Diligence and Funding Proposal process is completed and sent to Seven Stars' Advisory Panel.

Seven Stars' Management undertakes a strict tick-box review process before proposing a firm or sector to the Advisory Panel. Only after a firm and case type have been fully reviewed and a file specifically prepared is it submitted to the Advisory Panel for review and verification.

5. Advisory Panel review

When a file has been sent to the **Advisory Panel**, it is under the assumption that the prospective Funding Partner's proposal represents a good opportunity for Seven Stars to realise a return. Therefore, Seven Stars' Advisory Panel operates with a "fail list policy," i.e. looking for reasons not to lend to the prospective Funding Partner. Whilst the Panel will not act as a de facto Investment Committee, the oversight capacity will allow the Advisory Panel to raise flags on any funding opportunity.

6. Advisory Panel approval and closing documents

Should the Advisory Panel approve the file for the prospective Funding Partner, it returns the file to Andrew Neal. Andrew then issues the following documents, in addition to any others as required:

- Closing documents
- Deed of Assignment or Debenture
- Funding Agreement
- Funding Guarantee

if applicable if Seven Stars is using a Debenture, this must be placed within 15 days for the Funding Agreement to proceed.

7. How Funding Partners access funds

Seven Stars follows a consistent and strict procedure when Funding Partners wish to draw down funds.

- a. Funding Partner sends a funding request detailing a list of cases they would like to fund, including the amount they wish to draw down, case type, volume, and expected returns from the cases in question.
- b. Seven Stars reviews the case files for which the Funding Partner is seeking funding, including:
 - i. **Random sampling of claimant files**, for retainer and all legal documents, including anti-money laundering verification.
 - ii. **Verification of After The Event Insurance policy**, where applicable, for the case type being funded.
 - iii. **Verification of case and claimant details.**

Seven Stars also conducts **random update sampling** on previous funding tranches, audits of the Funding Partner's case book and case files, and how the claims we're funding are progressing.

These checks also enable Seven Stars to gather data for internal use to understand the overall business position and when returns may be realised. This data can subsequently be communicated to investors and used to inform future lending decisions with existing and prospective Funding Partners.

SUMMARY TABLE

RISKS	MITIGATION
Market	UK a favorable legal environment - UK judicial system considered one of the best in the world Clear legal precedents Only fund UK SRA regulated Law Firms or FCA Regulated CMC's Strong market growth
Cases Unsuccessful	Extensive internal & external due diligence Diverse portfolio of precedent based small consumer claims – predictable outcomes – 30/30 rule limits exposure to any one case type Minimum case values established ATE Insurance in place Continuous audit (Internal & external agencies) Seven Stars Legal loan repayment not dependent on case outcome
Case Settlement Delays	Diverse portfolio of precedent based small consumer claims – predictable outcomes – 30/30 rule limits exposure to any one case type or Law Firm
Law Firm Default	Extensive due diligence both internal & external agencies Full recourse lending Senior Security in place – Debenture/Deed of Assignment Continuous audit (Internal & external agencies) SRA Indemnity Fund Law firm PII policy
Debt Security Risk	Senior security in place – Debenture/Deed of Assignment Security must be a minimum of 1.5 times funds borrowed Minimum case values established – sufficient revenue to cover the loan ATE insurance in place



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