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Beyond Champerty:
The Rise of Third Party Litigation Funding

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I. Third Party Litigation Funding

From its humble beginnings in the United States twenty years ago, third party litigation funding is clearly on the rise. A 2017 survey found that nearly 30 percent of attorneys in private practice had used alternative litigation funding compared to a mere 7 percent a few years earlier. Interest in third party litigation funding has also been spurred by the increased cost of commercial litigation, notably intellectual property disputes, and the interest of corporations in removing litigation exposures from their balance sheets. Finally, there has been a significant uptick in publicity and press reporting concerning third party litigation funding in the wake of the disclosure that Silicon Valley billionaire Peter Thiel secretly underwrote the cost of Hulk Hogan's suit against the Gawker web site for distributing a private sex tape.

In 2016, the Wall Street Journal reported[1] that Los Angeles trial lawyer Raymond Boucher, architect of a $660 million settlement for California clergy-abuse victims, has taken out several million dollars in funding from publicly-traded litigation financer IMF Bentham. The Journal has separately reported that pension funds, university endowments, and private offices "have collectively pumped more than a billion dollars" into litigation finance vehicles.

The rise of third party litigation funding has not come without obstacles, however. As discussed below, many jurisdictions and corporate interests have sought to block or limit this practice on the basis of old common law doctrines, such as barratry, champerty and maintenance. In recent years, however, many of these obstacles have fallen away. Indeed, there is a substantial body of academic literature that proclaims the virtues of third party litigation funding and questions why involving third parties in funding litigation should be more dangerous or ethically problematic than allowing insurers to control and pay for the defense of civil law suits.

In this paper we will explore the current contours of the third party litigation funding debate and its potential implications for the future rights of insureds and insurers.

II. Common Law Antecedents: Barratry, Champerty and Maintenance

"Barratry" is the practice of filing vexatious litigation. During the Middle Ages, the authorities could prosecute individuals who "stirred up" litigation by encouraging plaintiffs to bring suit. "Maintenance" is "an officious intermeddling in a suit that in no way belongs to one, by maintaining or assisting either party with money or otherwise, to prosecute or defend [the suit]." Thus, *any* third-party support for a lawsuit theoretically constitutes maintenance. "Champerty" is a form of maintenance that involves "maintaining a suit in return for a financial interest in the outcome." "Because money is solicited from disinterested parties to fund litigation," usually in return for a share of the proceeds, "syndicated lawsuits, by

[1] https://www.wsj.com/articles/litigation-financing-attracts-new-set-of-investors-1463348262

definition, constitute champerty." As the U.S. Supreme Court succinctly declared in ***In re Primus,*** 436 U.S. 412, 424 n. 15 (1978):

> Put simply, maintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty.

Champerty and maintenance began in antiquity with the Greek view that even a party's advocate should have a personal interest in the litigation, such as family ties. Max Radin, *Maintenance by Champerty,* 24 Cal. L. Rev. 48, 49 (1935). During the Middle Ages, the antipathy of the English clergy and royals to lawsuits, particularly in secular courts, combined with fear that English barons would purchase land with clouded title to increase their estates and otherwise abuse the legal process by purchasing meritorious claims for insignificant amounts from plaintiffs too poor to prosecute their own actions resulted in royal regulation of champerty and maintenance. *Id*. at 64-66. These "champertors" had paid retainers – known as "maintainers" – prosecuted the suits ruthlessly on their behalf, taking "all necessary steps to win." Because kings soon found themselves the target of this vexatious litigation, and because of a general distaste for litigation in general, laws against champerty and maintenance were born.

III. Relaxation of Traditional Restraints on Third Party Litigation Funding

As medieval suspicion of litigation gave way to the age of commerce, most of these old-fashioned limitations on champerty and maintenance have been relaxed or abandoned. Traditional bars to champerty were set aside by the Australian High Court and courts in the United Kingdom in the earlier years of this century. With the removal of common law bars to litigation finance, markets were free to develop. The fact that Australia and the United Kingdom are so far ahead of the United States with respect to the evolution of alternative litigation financing may well reflect the fact that both have "loser pays" judicial systems, whereas in the United States, both parties typically are responsible for their own costs and attorney's fees. Additionally, Australia did not permit contingency fee arrangements of the sort that have commonly permitted injured individuals with limited assets to seek recovery against well-funded corporations in the U.S. and elsewhere.

In recent years, U.S. courts have largely relaxed earlier restrictions with respect to the ability of a plaintiff to assign a chose in action. Such suits may be assigned as a matter of right or contract pursuant to insurance policies, for instance, thus allowing insurers to pursue subrogation actions arising out of losses that they have paid on behalf of their policyholders. Beyond the insurance context, however, courts have frequently permitted plaintiffs to assign a chose in action even for claims that are personal to the plaintiff such as malpractice or invasion of privacy.

South Carolina, Massachusetts, New York and West Virginia, have significant limitations on champerty, while others – Arizona, California, Louisiana, New Jersey and Texas – either never adopted it or have since abandoned it. See Bond *Comment Making Champerty Work: An Invitation to State Action*, 150 U. Pa. L. Rev. 1297 (2002) (fifty state survey).

In *Saladini v. Righellis*, 687 N.E.2d 1224, 1226 (Mass. 1987), Righellis obtained a loan from Saladini to help him pursue legal claims arising from his interest in certain real estate. Saladini made the loan in return for a contingent interest in the recovery: his loan principal would be repaid from the first proceeds, plus he would receive 50% of any net recovery after attorney's fees. When Saladini attempted to enforce this agreement, Righellis defended by invoking champerty and maintenance.

The Supreme Judicial Court of Massachusetts rejected this defense, declaring that it was "no longer persuaded that the champerty doctrine is needed to protect against the evils once feared: speculation in lawsuits, the bringing of frivolous lawsuits, or financial overreaching by a party of superior bargaining position. . . ." The court noted that the view of litigation as "social ill" is long outdated. It also recognized that application of the champerty doctrine would provide the litigant with a windfall: Righellis would get to keep the litigation proceeds, while Saladini, whose financial contribution made the recovery possible, would end up with nothing. According to the court, fee regulations, sanctions rules, and the doctrines of unconscionability, duress and good faith are more than sufficient to prevent the "evils" that champerty was originally designed to address. Financing arrangements, the Court continued, should be analyzed on a case-by-case basis, with a focus on "whether the fees charged [are] excessive or whether any recovery by a prevailing party is vitiated because of some impermissible overreaching by the financier."

Likewise, in South Carolina, the state Supreme Court ruled in *Osprey, Inc. v. Cabana Limited Partnership,* 532 S.E.2d 269, 279 (S.C. 2003) that, "We abolish champerty as a defense because we believe it no longer is required to prevent the evils traditionally associated with the doctrine as it developed in medieval times." Restrictions on champerty were also set aside by the Kentucky Supreme Court in *McCullar v. Credit Bureau Systems*, 832 S.W.2d 887 (Ky. 1992).

Nevertheless, a significant number of states continue to maintain traditional restrictions on champerty and maintenance. For instance, in Minnesota, courts have declared that, "An agreement in which a party had had no interest otherwise, and when he is in no way related to the party he aids, is champertous and void as against public policy." *Johnson v. Wright,* 682 N.W.2d 671, 678 (Minn. Ct. App. 2004). Similarly, in Delaware, courts have declared that, "It is the duty of court to dismiss a case in which the evidence discloses that the assignment of the cause of action sued upon was tainted with champerty." *Hall v. State,* 655 A.2d 827, 829-30 (Del. Super. Ct. 1994).

In June 2003, however, the Supreme Court of Ohio dealt a severe blow to the litigation funding industry. In *Rancman v. Interim Settlement Funding Corp*., 789 N.E.2d 213 (Ohio 2003), the court ruled that a funding company's advance to a litigant in return for a percentage of the recovery was void under principles of champerty and maintenance.

Rancman had been seriously injured in a car crash, and had sued an insurance company for damages. Apparently in need of funds while the case was pending, she contacted Interim Settlement Funding Corporation ("Interim") to obtain a cash advance secured by her pending claim. Interim agreed to advance her $6,000 in exchange for the first $16,800 she would recover if the case resolved within 12 months, with higher payments due if the case took longer to resolve. If she did not obtain a recovery, she would pay nothing.

Rancman settled the case for $100,000 within 12 months, but refused to pay Interim the amount due under the contract. She eventually sued for rescission, and prevailed in the lower court on the ground that Interim's advance constituted a usurious loan.

On appeal, Interim argued that the advances were not loans at all, but investments (since there was no absolute obligation to repay). The Supreme Court of Ohio ruled that "[t]he advances here are void as champerty and maintenance regardless of whether they are loans or investments." The advances constituted champerty because "Interim sought to profit from Rancman's case," and constituted maintenance because Interim "purchased a share of a suit to which [it] did not have an independent interest" through an arrangement that "provided Rancman with a disincentive to settle her case."

Specifically, the Court noted that Rancman, in return for her $6,000 advance, had to pay Interim the first $16,800 she received in settlement and also had to pay her lawyer a 30% contingency payment. Thus, she would pocket nothing for herself unless the settlement exceeded $24,000. According to the Court, this created "an absolute disincentive" to settle for a lower amount, and resulted in prolonging the litigation. Meanwhile, the court concluded, Interim earned a "handsome profit by speculating in a lawsuit."[2]

Champerty also remains viable in many states pursuant to common law. In a recent Nevada case, for instance, the District Court observed that:

> Although champerty has not been a tort in England since 1967, *see* Criminal Law Act, 1967, c. 58, § 13(1)(a) (Eng.), unless superseded by state or federal law, the common law of Nevada is the statutory and common law of England as it existed at the signing of the Declaration of Independence. . . . Notably, although the Criminal Law Act of 1967 eliminated champerty as a crime and tort, it remains a valid contractual defense within the United Kingdom. . . . And even if the United Kingdom had eliminated champerty as a contractual defense, by statute the fork in the road between the common law of England and that of Nevada was the signing of the Declaration of Independence, and the Nevada Supreme Court explicitly reaffirmed the contractual defense of champerty less than fifteen years ago. *See Schwartz v. Eliades,* 939 P.2d 1034, 1036–37 (Nev. 1997) ("Although we concluded above that the district court erred by finding champerty, had there actually been a champertous agreement, Eliades would not have been entitled to restitution of the money he paid under the void agreement."). In

[2] Ohio has since enacted a statute regulating champerty practices.

> fact, this language indicates that in Nevada a champertous agreement is not only voidable, but void.

Incline Energy, LLC v. Penna Group. LLC, 2011 WL 1304710 (D. Nev. Apr. 1, 2011).

Legislative efforts to reinstate limitations on champerty failed in Texas in 2007 when the Texas Senate failed to approve House Bill 2987. In 2013, the Texas Legislature proposed a statute that would significantly limit the ability of third-party financiers to fund litigation by characterizing such agreements as a form of consumer legal funding subjecting it to interest rate limitations.

Efforts at reform also failed in Illinois several years ago when the state House voted 87-28 to kill the so-called “Law Suit Loan Shark Act.” Senate Bill 3322, the Non-Recourse Civil Litigation Funding would have:

> Provides that all contracts for non-recourse civil litigation funding must meet specified criteria. Provides that the contract shall provide that the consumer may cancel the contract within 5 business days following the consumer's receipt of funds, without penalty or further obligation. Specifies the notice requirements for contracts. Contains provisions concerning the dispute of contracts. Provides that each non-recourse civil litigation funding company shall adhere to specified best practices. Contains provisions concerning (1) the sale and assignment of proceeds of legal claims and (2) the requirements for non-recourse civil litigation funding companies by the Department of Financial and Professional Regulation. Provides that the Department shall maintain a list of all non-recourse civil litigation funding companies. Contains provisions concerning the power of the Department to issue cease and desist orders. Specifies penalties for violation of the Act. Contains provisions concerning judicial review and application of the Act. Amends the Consumer Installment Loan Act to exclude non-recourse civil litigation funding

It has been reported[3] that Florida, Ohio, New York and Texas are the states that are most accommodating to third party financing of litigation. Conversely, Alabama, Colorado, Kentucky, and Pennsylvania are among the states that are most hostile to it.

Fifteen states still enforce common law prohibitions against maintenance in champerty. See *Johnson v. Wright*, 682 N.W.2d 671 (Minn. App. 2004) and *Fleetwood Area School District v. Berks County Board of Assessment Appeals*, 821 A.2d 568 (Pa. Super. 2003). Conversely, 28 states and the District of Columbia permit litigation funding with certain limitations including Delaware, New York and California.

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[3] “The Best and Worst States for Litigation Finance” (Above the Law 2017). http://abovethelaw.com/2017/07/the-best-and-worst-states-for-litigation-finance-part-ii/

Other states continue to maintain restrictions on champerty but do so in a sense that appears more geared towards preventing barratry as by focusing on whether the third party was instrumental in the decision to bring the lawsuit as opposed to merely facilitating its prosecution. *See Bluebird Partners, L.P. v. First Fidelity Bank, N.A.,* 94 N.Y.2d 726, 731 N.E.2d 581 (2000). Such claims are still barred by Judiciary Law §489, which provides in pertinent part:

> **Purchase of claims by corporations or collection agencies**
>
> No person or co-partnership, engaged directly or indirectly in the business of collection and adjustment of claims, and no corporation or association, directly or indirectly, itself or by or through its officers, agents or employees, shall solicit, buy or take an assignment of, or be in any manner interested in buying or taking an assignment of a bond, promissory note, bill of exchange, book debt, or other thing in action, or any claim or demand, with the intent and for the purpose of bringing an action or proceeding thereon.

In 2017, Vermont became one of the first states to specifically regulate third-party litigation funding. House Bill 84 requires litigation funders to be licensed in Vermont and to post a letter of credit or a surety bond to protect consumers. On the other hand, neither the licensing requirements or the amount of the bond are particularly onerous.

In 2016, the Delaware Superior Court rejected efforts to dismiss an intellectual property suit as violating the rules against champerty. In *Charge Injection Technology Inc. v. E.I. DuPont*, (Del. Super. 2016), Charge Injection Technologies ("CIT") had alleged DuPont wrongfully used and disclosed CIT's technology. After years of expensive IP litigation, CIT turned to Burford Capital for financial assistance in return for a percentage of any eventual recovery. Burford also received a security interest in CIT's claims as collateral.

Upon learning of Burford's suit, DuPont moved to dismiss CIT's on the grounds of maintenance and champerty. The Superior Court declined to grant DuPont's motion to dismiss but did allow it to obtain discovery with respect to CIT's funding arrangements. Following this discovery, DuPont again moved to dismiss. In early 2016, Judge Jurden refusing to grant the motion to dismiss, declaring that, "[t]he court is not persuaded by DuPont's argument that the [claim] is champertous because of Burford's alleged de facto control. …The record before the court demonstrates that CIT is the bona fide owner of the claims in this litigation, and Burford has no right to maintain this action." Crucially, the Superior Court found that CIT was still the real party in interest as it had not assigned its claims to Burford and that, apart from having certain rights with respect to decisions concerning selection of counsel, Burford the express or *de facto* right to direct, control or settle the claims. Further, the court observed that CIT had pursued this litigation for five years before Burford's involvement and that there was no evidence had incited the litigation or otherwise encouraged CIT to pursue frivolous claims.

IV. The Rise of Modern Third Party Litigation Funding

The renaissance of third-party litigation funding began in Australia several decades ago during a period of time when Australia prohibited contingent fee arrangements in Australia. In the decades since, it has spread to the United Kingdom and, to a significantly lesser but growing extent, Europe and North America.

At its simplest level, ALF is little different from a private mortgage that a consumer may obtain to purchase a home where bank financing is unavailable due to the consumer's poor credit history. In its more sophisticated forms, however, ALF investors may securitize such risks or invest in them through devices such as hedge funds. In the future, some of these loans may even be financed through public companies financed through stock offerings.

Modern third party litigation funding may take one of three forms:

> *Loans*: In the first type, the financier simply loans a certain amount of money to the plaintiff in consideration of the repayment of that loan and interest. In such instances, the financier exerts little or no control over the handling of the litigation.
>
> *Litigation Financing*: In large intellectual property cases or other types of commercial litigation lawsuits, the financier agrees to fund some or all of the costs of the litigation in consideration of a significant percentage recovery from the eventual outcome of the lawsuit. Thus, a financier may loan 50 percent of the cost of litigation in consideration of 20 percent of any recovery. In these cases, the financier requires far more information with respect to the ongoing handling of the case and may or may not take a direct role in strategic or settlement decisions.
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> *Portfolio Loans:* Finally, there are so-called pool or portfolio arrangements where a financier may loan money to a law firm or a party involved in a large group of cases. Pool investing allows the financier to distribute its capital among numerous different cases that a law firm might be handling, thus diversifying the risk to the funder. In such instances, the financier balances its risk across the entire portfolio of law suits being handled by the firm, much in the way that an investor in the stock market may face less risk by placing money into a mutual fund and buying individual stocks.

In portfolio funding cases, the financier will provide a law firm with funds for a group of cases and will take its fee from the collective result rather than the individual disposition of each case. As an investment prospectus from Jersey-based Burford Capital proclaimed:

> Burford Capital's strategy is to create and manage a portfolio of commercial dispute financing investments diversified by duration, claim type, geography and a number of other variables, with the aim of providing shareholders with attractive levels of dividends

> and capital growth. The Company expects returns to be uncorrelated to general equity market performance.

The U.S. litigation financing market is dominated by two companies: Juridica Capital Management and Burford. In addition to Burford, other prominent litigation financiers include Juridica Capital, Calunius Capital, Juris Capital, Arca Capital, and IMF. Additionally, a few banks, notably Credit Suisse and Deutsche Bank have units that specialize in litigation financing

These financiers rarely invest in personal injury cases and tend to focus on large commercial cases where the amount in dispute exceeds $25,000,000. Some funders also provide support to defendants against various types of negative results, including the obligation to pay attorney's fees in "loser pays" jurisdictions.

Apart from funders such as Burford and Juridica, there have been reports of instances where private individuals funded litigation, as in Hulk Hogan's notorious suit against Gawker for publishing his sex tape. Additionally, some private citizens are raising money for their lawsuits through crowd-funding events. At the end of 2016, for instance, the Green Party nominee for president, Jill Stein, raised several million dollars to fund recount challenges in Wisconsin and other battleground states.

Finally, several startup companies in the United States have become involved in crowd-funding litigation, including LexShares, Trial Funder and Invest4Justice. These companies list various law suits on their web sites that they have already vetted and offer opportunities for individual investors to fund at a significant lower cost that the major law suit funds. Invest4Justice has received several million dollars since it was founded in early 2014. At the time of its founding in April 2015, Trial Funder's CEO declared that its mission was to assist plaintiffs in civil lawsuits involving police brutality, sexual harassment, wrongful death and other personal injuries "Trial Funder promises to democratize the legal system, while bringing a new level of transparency to the entire process." Mighty Group has reportedly helped to fund over 1000 suits already.

V. How Are ALF Loans Different From Contingent Fee Agreements?

Notwithstanding these concerns, the original idea that a party should be solely responsible for its own litigation costs has already been substantially eroded. In America, contingent fee agreements that entitle a plaintiff's lawyer to recover as much as 40% of his plaintiff's ultimate recovery are quite common in personal injury litigation. Likewise, in large class action suits and mass tort litigation, it is not at all uncommon for well-known plaintiffs' firms to merge their assets, intellectual and otherwise, to finance and prosecute class action claims. If the lawyer prosecuting a case is entitled to invest in it, what then is the danger of allowing disinterested third parties to do so?

Traditional restrictions on client funding have largely been relaxed over the years on the basis that they facilitate access to justice particularly on the part of individual citizens or plaintiffs who might not otherwise be able to afford competent counsel through their own resources. As a result, plaintiffs' law firms are allowed to enter into contingent fee agreements with their clients where the client is still obligated to pay the cost of the litigation but the lawyer agrees to only accept a fee based upon a percentage of the ultimate recovery.

The key difference between contingent fee agreements and alternative litigation financing is that a lawyer agrees to provide a service for a fee in a contingent fee agreement whereas litigation financing involves an investment in an asset by a third party.

Litigation finance entities are also not subject to the Rules of Professional Responsibility that govern the conduct of law firms in the individual jurisdictions making up the United States. Accordingly, they may be guided by profit and business strategy decisions without necessarily being concerned about conflicts of interest that would otherwise prohibit a law firm from becoming involved.

In the past, mass tort litigation in the United States has often been financed through consortia of well-established law firms specializing in such work, who shared their resources to pioneer such claims. Even these fee sharing arrangements have proved problematic in some cases. For instance, in *In Re: Agent Orange Products Liability Litigation,* 818 F.2d 216, 217 (2nd Cir. 1987), certain of the lead law firms pursuing the Agent Orange case agreed to fund the cost of the litigation in return for a 300% return on their investment before funds were distributed to the remaining firms. Although a federal district court in New York agreed to the arrangement, finding that there was no evidence that it had affected the willingness of the parties to settle, it was set aside by the U.S. Court of Appeals for the Second Circuit. The Court of Appeals held that fee sharing arrangements "that include a return on investment present the clear potential for a conflict of interest between class counsel and those whom they have undertaken to represent."

VI. How Is Third Party Funding Different From Liability Insurance?

For more than a century, defendants in civil suits have had their legal fees financed by liability insurers. Why then, should there be concerns about third parties funding the prosecution of civil suits?

There are several key differences between liability insurance and third-party litigation funding, however. First and foremost, insurance contracts are designed to minimize liability costs whereas funding arrangements are intended to maximize liability recoveries. Second, insurance policies are issued prior to any loss occurring whereas third-party litigation funding is negotiated after a loss has already incurred in anticipation of a lawsuit and eventual recovery on account of that loss. Third, whereas insurers are required to defend all covered claims, financiers may pick and choose among those that they seek to support. Finally, a consumer who enters into a contract with a third party financier has some degree of certainty of assistance, whereas a policyholder cannot always know that a liability insurer will agree to defend or whether the insurer will either deny coverage or reserve its rights with respect to certain aspects of the claims.

Professor Charles Silver of the University of Texas made an aggressive argument in favor of the similarities between liability insurance and third-party litigation funding in his 2014 article in the DePaul Law Review. In his article, Silver pointed to the example of how insurers minutely manage litigation and argued that the involvement of third parties in litigation or settlement decisions will not necessarily skew the judicial process or result in inequity to any party.

Silver also argued that both funding mechanisms have much in common. Liability insurance and third-party litigation funding are both subject to adverse selection as insurers seek to avoid poor risks whereas financiers are careful to only loan money for worthwhile lawsuits. Silver observes that third party funders will only invest in large commercial litigation after an investigation period that could last up to 90 days and cost $75,000 to $100,000.00 for each screening.

There is, in fact, something resembling a parallel tripartite relationship in context of third-party litigation funding involving the financier, the client and a law firm. Unlike the traditional tripartite relationship among insurers, policyholders and defense counsel, however, it is typically not the financier that hires counsel or specifically controls the litigation.

Silver's 2014 article was written in response to a 2012 article by Professor Michelle Boardman in the Journal of Law Economics and Policy in which she identified five key differences between liability insurance and lawsuit funding: 1) contractual relationship between the policyholder and the liability insurer precedes the litigation; 2) the insurer's involvement in the litigation is automatic, not an investment choice; and 3) the litigation funding is the primary purpose of the contract; 4) the policyholder has a duty to cooperate with the insurer; and 5) the policyholder and the insurer are co-clients of defense counsel.

Boardman's critique was echoed in a white paper[4] released by the National Association of Mutual Insurance Companies in 2011 in which NAMIC argued that there are fundamental differences between the involvement of liability insurers in defending lawsuits and the involvement of third-party financiers in funding litigation. "Whereas the primary objective of funding companies is to promote and profit from litigation, insurers seek to avoid litigation and minimize its costs."

VII. Criticisms of Third Party Litigation Funding

Third-party litigation funding arrangements have come under harsh criticism from the U.S. Chamber of Commerce and insurer advocates in recent years.

In 2012, the Institute for Legal Reform arm of the U.S. Chamber of Commerce issued a White Paper[5] recommending that the federal government adopts rules (1) prohibiting investor control of cases; (2) forbidding direct contracts between investors and lawyers that do not also include the client; (3) banning law firm ownership of third party financing firms; (4) prohibiting the use of financing in class actions; and (5) requiring disclosure of funding contracts in litigation.

[4] National Association of Mutual Insurance Companies: *Third Party Litigation Funding: Skipping The Scales of Justice for Profit* (NAMIC Issue Analysis: May 2011).

[5] U.S. Chamber Institute for Legal Reform, *Stopping the Sale on Lawsuits: A Proposal to Regulate Third-Party Investments in Litigation* (Oct. 2012)

In its 2011 White Paper, NAMIC criticized such funding arrangements as "tipping the scales of justice for profits" and expressed concern that "litigation funders will naturally seek to exert control of those strategic decisions that affect their litigation portfolios." NAMIC also expressed concern that the growing involvement of third-party litigation funding would result in more lawsuits being filed and making it more difficult to settle such claims, thus increasing the overall cost of the litigation system. NAMIC noted that placing greater financial resources in the hands of plaintiffs would allow them to undertake to hire litigation communications consultants who specialize in "orchestrating negative media campaigns aimed at defendants" that would result in unfair reputational damage to defendants and place greater pressure on them to settle otherwise unmeritorious cases. NAMIC darkly predicted that third-party litigation funding would encourage more frivolous lawsuits and over time would skew the evolution of tort law by enabling plaintiffs' law firms to litigate strategically.

The NAMIC White Paper concluded with the following recommendations:

1. Third-party funding should not be allowed in class action settings or to finance mass tort litigation.

2. Interest rates on funds advanced under third-party financing arrangements must be limited to "a reasonable" amount.

3. Third-party funding must be restricted to actions by individual plaintiffs for torts involving personal injury.

4. The amount that can be taken as loan repayment from the net recovery should be limited to a percentage of the net recovery.

5. Litigation funding companies should not be allowed to make referrals to attorneys on behalf of a potential plaintiff, nor accept advertising from attorneys on their web sites or in their marketing materials.

6. Attorneys should not be allowed to have a financial interest in the litigation funding company.

7. Litigation funding companies should not be allowed to exert influence over the plaintiff's decision to settle or to otherwise direct the court of litigation.

8. The existence of any third-party funding arrangement should be disclosed to all parties to the lawsuit and to the court.

Other groups have expressed concern that third party litigation funding creates ethical quandaries for lawyers and may distort the future course of litigation.

A. Ethical Concerns

A White Paper released by the ABA Commission on Ethics 20-20[6] last year expressed concern with respect to the potential impact on third-party litigation funding arrangements for lawyers involved in such cases. The White Paper suggested that such arrangements might implicate the following rules of professional responsibility:

- Model Rules 1.7(a)(2) (representation material be limit by lawyer's responsibility to a third party or the lawyer's own interests).

- Model Rule 1.8(e) (lawyers may not provide financial assistance to client).

- Model Rule 1.8(f) (lawyer must not accept compensation for representation from third party without informed consent of client and unless it will not interfere with independent professional judgment).

- Model Rule 1.8(i) lawyer may not acquire propriety interest in subject matter representation)

- Model Rule 5.4(c) (the lawyer may not permit fee pay or direct or regulate lawyer's professional judgment).

The White Paper suggested that lawyers might be put in an ethical bind if they were prosecuting a claim where the third-party litigation funding gave the financier the right to cut off further funding in the event of certain strategic decisions contrary to the financier's interests. In such circumstances, counsel "may reasonably believe that the funder's second guessing of decisions made in the representation of the client is an unreasonable interference with the lawyer's professional judgment." The ABA White Paper also expressed concern that such arrangements might endanger the confidentiality of attorney-client communications and otherwise violate Model Rule 1.6(a).

B. Do ALF Arrangements Generate More Lawsuits?

As third party litigation funding is only in its infancy in the United States, there is little empirical to support or refute concerns that it is generating increased law suits, encouraging frivolous litigation or otherwise changing the arc of litigation in this country.

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[6] American Bar Association Commission on Ethics 20/20: *White Paper on Alternative Litigation Financing* (2016).

Some guidance may be derived from the experience of Australia, which has had a much longer experience with these funding arrangements than Europe or the United States. In a landmark study[7] published by the University of Pennsylvania Institute for Law Economics, David Abrams and Daniel Chen found that jurisdictions with a larger number of financed law suits tended to have a bigger back log as such suits were less likely to settle and dragged on longer. The authors suggested that this backlog might be temporary, however. They pointed out, moreover, that financed cases also tended to be more important and were more likely to generate results of precedential value.

Abrams and Chen's paper also tends to undercut claims that litigation financiers are likely to spawn more frivolous litigation. Their review of the records of IMF Bentham, which has a 50% market share of ALF in Australia, indicate that between 1999 and 2007, the financier received 763 proposals but only agreed to fund 91 cases. To similar effect was a 2016 story in the Wall Street Journal that reported that one financier rejected 95% of the cases presented to it for funding.[8] Proponents of third party litigation funding point to these figures as evidence that funding is not promoting frivolous litigation and these funding companies are only investing their money in worthwhile cases for which there is a good chance of a favorable result.

VIII. Criticisms of Third Party Litigation Funding

A. Legal Challenges

A. Client Claims of Champerty

As detailed above, ALF borrowers may have good grounds for disputing ALF arrangements in states that continue to maintain common law or statutory rules against champerty and maintenance.

B. Defendants' Challenges To Champerty

U.S. courts remain divided with respect to whether champerty is a defense that only a party to an unconscionable agreement may raise or whether third parties may seek to set aside champertous agreements that affect them. In short, may a defendant who is being sued as the result of litigation being financed through champertous means seek to void that agreement?

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[7] David S. Abrams and Daniel L. Chen, *A Market for Justice: A First Empirical Look at Third Party Litigation Funding*, 15 U. Pa. J. Bus. L. 1075 (2013)

[8] Sara Randazzo, *Litigation Funding Moves into Mainstream*, WALL STREET JOURNAL (Aug. 4, 2016)

In *CSX Transportation, Inc. v. Gilkison,* 406 Fed. Appx. 723 (4th Cir. 2010), a U.S. railroad sued certain plaintiffs' law firms claiming that they had engaged in common law fraud and civil conspiracy and had violated the Racketeer Influenced and Corrupt Organizations Act (RICO) by fabricating and prosecuting objectively unreasonable, false and fraudulent asbestosis claims against it. Although these claims were largely vacated by the U.S. District Court, they were reinstated late last year by the U.S. Court of Appeals for the Fourth Circuit. The suit alleged that the plaintiffs' firms had engaged in an illegal conspiracy with physicians who fabricated x-ray screenings to support allegations of asbestosis.

In *Dell Webb Communities, Inc. v. Partington,* 2011 WL 2854086 (9th Cir. July 20, 2011), a U.S. District Court in Nevada enjoined a building inspection company that sought to detect construction defect problems which it referred to various local law firms in return for a finder's fee that varied depending on whether the homeowner merely signed an engagement letter or prevailed in its suit. The District Court held that these agreements violated Nevada's common law prohibition against champerty and maintenance as the building inspection company was, in effect, using its own funds and resources to instigate and prosecute actions in which it had no interest. On further review, the U.S. Court of Appeals for the Ninth Circuit ruled that the defendant had no standing to dispute the efficacy of the financing arrangement, as it was not a party to this contract. The Ninth Circuit found that there was no basis for predicting that the Nevada Supreme Court would recognize a common law tort cause of action for damages or equitable relief asserted by a stranger to an allegedly champertous agreement.

B. ALF v. Syndication

Even the *Saladini and Osprey* courts made clear that their decisions "should not be interpreted to indicate our authorization of the syndication of lawsuits." While neither court gave any reason for limiting its holding in this way, it appears that even these pro-financing courts view multi-investor arrangements, which may involve huge sums of money and the public solicitation of lay investors, very differently from private, one-on-one arrangements designed to help one impoverished litigant.

C. Ethical Issues

1. Prohibition Against Fee Splitting With Lawyers

The growing popularity of alternative litigation finance arrangements has resurrected issues with respect to the impropriety of non-lawyer professionals being affiliated with lawyers. While the barriers to law firm affiliations with non-lawyers eroded throughout the 1990s, any momentum in this regard largely dissipated in the wake of Enron and other scandals in the past decade involving the big eight accounting firms.

Rule 5.4 of the American Bar Association's Model Rules of Professional Responsibility states that, "A lawyer or law firm shall not share legal fees with a non-lawyer." The intent of the rule is to protect lawyers from having others infringe upon the exercise of their professional judgment. As a consequence of this rule, American law firms have been constrained with respect to the extent to which they can be directly affiliated with accountants or other professionals. Such constraints seemed to be on the wane in the 1990s but gained fresh currency following the collapse of Enron and the ensuing scandals that tainted the reputation of the former big eight accounting firms in the years that followed.

It has been argued that ALF financing arrangements avoid Model Rule 5.4 because the lawyer is not sharing his fee with a third party. Rather, such arrangements are undertaken directly between the client and the financing entity and are generally exclusive of the fee owed to the lawyer.

2. Exchanging Confidential Information

If the litigation financiers are not clients, to what extent are they entitled to information concerning the status of the litigation or reports from defense counsel without waiving the otherwise privileged content of such communications? May litigation financiers claim a common interest in the litigation such that they are entitled to receive such reports much like excess insurers have been permitted to in the United States even though they are not the entity represented by counsel or even paying for counsel's services?

Different financiers have different requirements with respect to the amount of information that they may require from a prospective client and their attorneys before deciding to grant funding for a law suit. Likewise, others may also require periodic conference with counsel or access to reports that clearly implicate the attorney-client privilege. This does not, however, preclude the use of the work-product doctrine or some form of the common interest doctrine to shield certain materials from discovery. *See Mondis Tech., Ltd. v. LG Elecs., Inc.*, 2011 WL 1714304 (E.D. Tex. May 4, 2011) (documents created for potential investors were protected by work-product) and *In re Int'l Oil Trading Co.*, 548 B.R. 825, 832 (S.D. Fla. Bankr. Apr. 28, 2016) (the attorney-client privilege is not waived if the "third party and the privilege holder are engaged in some type of common enterprise and [] the legal advice relates to the goal of that enterprise").

3. Conflicts of Interest-Public Disclosure

Among the unanswered questions is the extent to which such litigation financing arrangements must be disclosed to all parties in the case or to the judge supervising the case. Relatively few of these arrangements see the light of day. A rare example is the involvement of Burford Capital in the lawsuit that Indian tribes in Ecuador filed against Chevron. In that case, Burford invested $4 million in the suit against Chevron in November 2010 in exchange for a 1.5% share in any recovery. Even if plaintiffs ultimately recover less than $1 billion, however, Burford is still entitled to recover its full $55 million promised payout unless the plaintiff's ultimate recovery is less than $69.5 million. In short, for an investment of a mere $15 million, Burford is entitled to a potential recovery of up to 80% of the plaintiffs' actual award or settlement.

Courts around the country are divided with respect to whether disclosure is required and on what basis. A few courts have permitted discovery. *See, e.g. Leader Tech., Inc. v. Facebook, Inc.*, 719 F. Supp. 2d 373 (D. Del. 2010) (common interest privilege does not apply to protect disclosures made to a litigation funder) and *Gharabe v. Chevron Corporation* (N.D. Cal. August 10, 2016) ordering plaintiff to produce funding agreement). Others have refused to require disclosure. *See Kaplan v. S. A. C. Capital Advisors,* 2015 WL 5730101 (S.D.N.Y. Sept. 10, 2015) holding that third-party litigation documents were not relevant to any claim or defense and thus not required for disclosure); *Miller UK Ltd. v. Caterpillar, Inc*., 17 F. Supp. 3d 711 (N.D. Ill. 2014) (financing documents are not discoverable because the funder was not the real party in interest);; *Devon IT, Inc. v. IBM Corp.*, No. 10-2899, 2012 WL 4748160 (E.D. Pa. Sept. 27, 2012) (common interest privilege applied to protect disclosures to a third-party litigation funder because the plaintiff and the funder shared a "common interest in the successful outcome of the litigation which otherwise [plaintiff] may not have been able to pursue without the financial assistance" of the funder).

Automatic disclosure of third-party litigation funding has also been considered by the Advisory Committee on Civil Rules since 2014 but, as yet, has not been adopted. Additionally, the amendments to the Class Action Fairness Act that were passed by the U.S. House of Representatives in March 2017 as the Fairness in Class Action Litigation Act of 2017 (HR 985) would have required prompt disclosure to U.S. district courts of third-party litigation funding in all class actions by any entity "with a contingent right to receive compensation from any settlement, judgment or other relief obtained in the action."

Pending amendments to the federal rules, lower courts are left to their own devices with respect to whether the fact and details of third-party funding must be disclosed. Only the U.S. District Court for the Northern District of California has promulgated a rule mandating automatic disclosure of third-party funding in certain cases. In June 2016, the Northern District proposed a change to Local Rule 3-15 that would have required automatic disclosure at the outset of litigation of any person or interest "with a financial interest (of any kind) in a subject matter in controversy or in a party to the proceeding." After vehement opposition by financiers, the court ultimately scaled down the scope of these revisions to Local Rule 3-15. In its final form promulgated in January 2017, disclosure of third-party litigation funding will only be required for class actions.

IX. The Future of Champerty and Maintenance in the United States

The control of champerty and maintenance in the United States has largely shifted from common law prohibitions against litigation financing towards treating these arrangements as another sort of consumer transaction requiring regulation and protection against predatory or usurious lenders akin to rules against usury.

As the scope of ALF funding becomes more sophisticated and widespread in this country, it is expected that new challenges will emerge, particularly from non-clients, focusing on ethical and confidentiality problems presented by ALF lenders who are more than mere lenders and who are taking an active role in litigation and settlement decisions.

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