Third-Party Financing of Class Actions: Recent Judicial Decisions, Ethical and Practical Considerations

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Introduction

- Today’s topic: class action (and therefore attorney-directed) litigation funding.
- We will also speak about client-directed litigation funding and about attorney-directed mass tort litigation funding.
- We may address potential new defense-side litigation funding options.
- Not covered: individual consumer/personal injury litigation funding.
In the Beginning . . . .

- Doctrines like champerty, barratry and maintenance, but also cases like *Brown v. Bigne*, 28 P. 11, 13 (Or. 1891):
  
  A fair bona fide agreement, by a layman, to supply funds to carry on a pending suit, in consideration of having a share in the property if recovered,...ought not to be regarded as *per se* void....Indeed, it may sometimes be in furtherance of justice and right that a suitor who has a just title to property, and no means except the property itself, should be assisted in that way.

- Developments in the U.K. and Australia precede the U.S. (and the sky has not fallen)
Today’s U.S. Litigation Funding Market

- Collateralized loans secured by a law firm’s receivables are still at the heart of most lawyers’ and firms’ financing.
- But there are problems caused by lawyers’ (and/or clients’) lack of access to capital.
- The growth and development of the U.S. claims transfer market.
- An “access to justice” issue but also a genuine financing and risk issue for lawyers and clients.
Nomenclature

- Litigation Finance
- Litigation Funding
- Third Party Funding
- Alternative Litigation Finance
- Commercial Claim Investing

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IT ALL STARTED WITH EDWARD LONGSHANKS, HAMMER OF THE SCOTS

- Maintenance
- Champertcy
- Speculation
- Usury

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700 Years of Randomness

Contingent Fees Permitted in the US
Contingent Fees Absolutely Illegal in England

Champerty De-criminalized in England
Champerty Criminalized in Mississippi

Loser pays rule in England
No Loser pays rule in US

Usury prohibitions abolished in England
Usury regulated in the US

All had impact on Access to Justice and Flows of Capital into law markets
Recent Developments

TPF Permitted by Legislation in England
Champertyp largely ignored in US States
Hedge and Private Equity Firms pouring into in Litigation
English Lawyers permitted to charge Contingent fees (DBAs)
Gambling increasingly legal in Common Law World
Interest charges common in the Islamic world
Derivatives of Derivatives
The Key Issues

- Stigma and the “Inauthentic Claim” (the stranger’s money should not flow to litigants or lawyers because it upsets the natural symmetries and balance of the justice process)
- Independent Professional judgment is fragile and will be compromised by the stranger’s money
- Client secrets cannot be preserved when strange money comes into the system
- The lawyer monopoly over “investments” in cases perpetuates the quarantine
Why Do Law Markets Want Capital?

Access to justice

Law firm capital demands

Complete or partial alternative to contingent fees

Liquidity for working capital or expenses

Risk hedge against assets of speculative value

Choice and Options
Who are Law Market Capital Participants?

Lawyers

Banks

Retail

Commercial

Ad hoc investors (funds, HNWIs and institutional investors)

Insurance companies

Brokerage/agents/intermediaries

How much has been invested?
How is Capital Entering the Law Market?

- Recourse or non-recourse loans to claim or judgment holders
- Direct purchases of interests of claim or judgment holders
- Recourse and non-recourse loans to lawyers secured by fees
- Hybrid litigation risk-sharing arrangements
- Derivatives: collars and floors
- Insurance products
Issues in Client-Directed Litigation Funding and How They are Addressed

- Conflicts of interest if lawyers represent the client in negotiations with the funder or if the lawyer wants to be the funder.
- Potential interference with client confidentiality and work product; defense ability to access.
- Potential interference with attorney judgment.
- Enforceability issues.
Why Should Lawyers, Instead of Clients, Direct Litigation Funding?

- Named class members can’t bind the class.
- Individual mass tort plaintiffs can’t borrow enough.
Issues in Class Action Litigation Funding and How They are Addressed

- Conflict of interest issues if the plaintiff’s firm represents the client(s) in negotiating with a funder.
- Potential interference with client confidentiality and work product; defense (and court) ability to access.
- Potential interference with attorney judgment.
- Enforceability issues.
- Disclosure to client issues.
- Enforceability issues.
- Fee splitting issues.
A Funny Thing Happened on the Way Through NYC

- NYC Bar Ethics Opinion 2018-5 and RPC 5.4(a).
- Contrary to recent New York caselaw.
- Contrary to much of history of RPC 5.4(a).
- Not revoked, but under further study.
- But see Comment [2] to New California RPC 5.4.
- Possible federal preemption argument.
Wrapping Up

- Other recent cases and opinions of note.
- On the horizon or already here: defense-side litigation funding.
Open Questions and Answers