Ethics and Commercial Litigation Finance

ACC Association of Corporate Counsel
CHICAGO

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Agenda

1. Background
   a) Financing commercial litigation
   b) Defining litigation finance and use
   c) How clients and law firms use litigation finance
2. Practical application
   a) Role of the funder and investment process
   b) Matters suited for funding: criteria
   c) Evaluating potential funders
3. Ethical considerations
   a) Champerty, maintenance, barratry
   b) Usury
   c) Control of counsel, strategy and settlement
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   e) Confidentiality
4. Discovery
   a) General overview
   b) Work product
   c) Attorney-client privilege
   d) Common interest exception
   e) Disclosure

Background

Definitions, types and uses

Financing commercial litigation

The financing of commercial litigation takes many forms

- Commercial plaintiffs may self-finance claims by drawing on existing credit sources, accessing venture capital, and seeking capital from investment banks, funds and private investors
- There is an active market in commercial claims; owners of claims can easily sell or assign them to economic actors interested in pursuing them
- The assets underlying claims (or related debt or derivative instruments) are frequently bought and sold to extract the value associated with the claim through litigation, in both insolvency and non-insolvency contexts
- Contingency fees for commercial claims are widely available, from both traditional contingency plaintiffs' firms and from many hourly firms
- Insurance and reinsurance are widely used in all stages of litigation process
- Over the past decade or so, specialist providers of litigation finance have joined this field, growing significantly as the demand for outside capital to finance commercial litigation has outstripped the supply from traditional sources

Defining litigation finance

Burford is the leader of this fast-growing field

- Value of litigation claims is used to obtain financing
- Capital is provided for case fees and expenses on a non-recourse basis, in exchange for return tied to case outcome
- Financial burden is lessened for litigants with fee fatigue or in need of alternative fee structures
- Used by firms to expand contingency fee or alternative fee practice, manage risk and cash flow
- Payment of litigation-related receivables can be accelerated

2018 Litigation Finance Survey

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Evolving use

Litigation finance is becoming corporate finance for law

- Litigation serves as collateral to provide capital that may be used for broader business needs beyond fees and expenses
- Used to unlock the asset value of litigation both by plaintiffs and by defendants
- Financing embraced by GCs and CFOs as a tool of choice, with significantly better impact on corporate balance sheets than paying out of pocket
- Embraced by firms of all types as a tool of choice, not necessity
- Increasingly moving from single case funding to financing portfolios of litigation and arbitration and other bespoke arrangements

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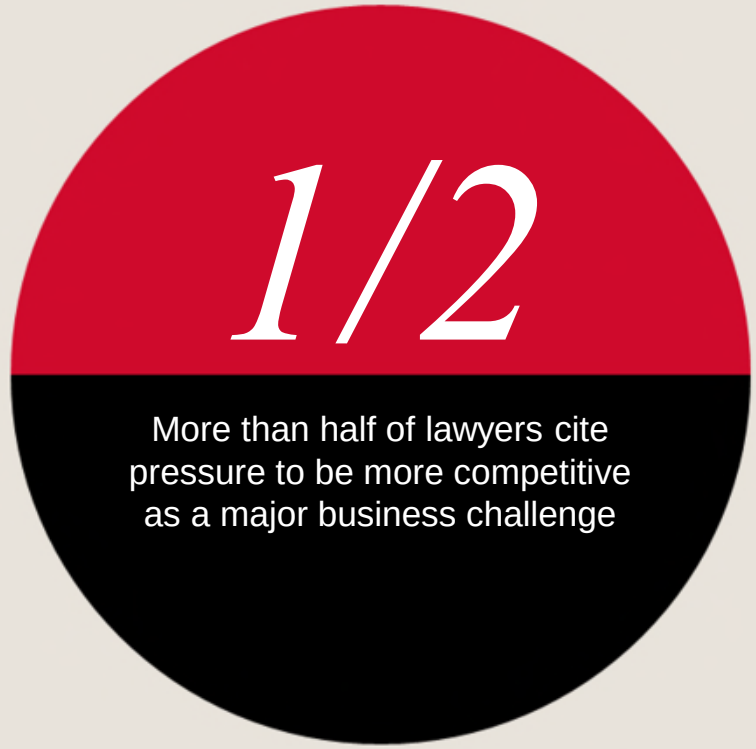
“Hundreds of companies, increasingly from the Fortune 500, have used litigation finance, convinced it was in their interest.”

– The New Yorker

How firms use litigation finance

Range of financial solutions for leading firms around the world

- Non-recourse capital to firms on a single case, portfolio or bespoke basis
- Enables firms to maintain hourly clients and expand into new areas
  - Functions as “synthetic contingency” for hourly clients under pressure to reduce fees
  - Enables hourly firms to pitch expanded service without increasing cost
- Enables firms to manage risk on large-dollar contingency or alternative fee matters
  - Reduce contingency risk for ongoing pre-trial litigation
  - Monetize expected fee after trial, pending appeal
- Aids law firm marketing development efforts
  - New business: Financing enables “no lose” proposal to expand current work with client into new areas
  - Beauty contests: Financing can be included in firm pitch to enhance success in competitive situations



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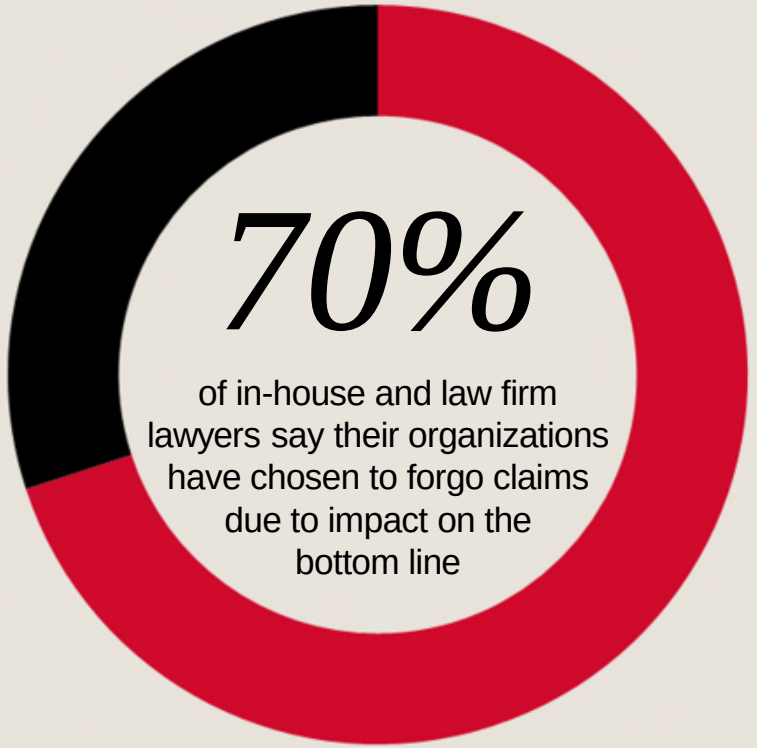
How companies use litigation finance

How companies from start-ups to the Fortune 500 are using litigation finance

- Value of litigation or arbitration claim is used to obtain financing
- Used by companies to
  - Fund legal fees or expenses
  - Finance portfolios of litigation
  - Transfer or share risk in matters
  - Monetize litigation assets at beginning of a case, or after judgment or appeal
  - Secure corporate debt facilities
  - Finance, sell, or collect uncollected judgments
  - Secure litigation-related insurance and risk solutions
  - Trace assets and enforce judgments against litigation debtors



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Practical application

Process, criteria, considerations

Role of funder

- No interference with lawyer/client relationship or obligations
  - Burford has no control over litigation strategy or settlement decisions
- Consideration of confidential and privileged information
  - Case law confirming work product protection applies to funder communications and documents
  - We're vigilant in managing diligence to avoid risking waiver of protected communications
- Reporting requirements for investments
  - Burford requires regular reporting of significant case developments
  - We may offer case-related advice but have no decision-making authority
- Investment process:
  - NDA
  - Initial case review
  - Due diligence
  - Ethical compliance
  - Investment approval
  - Negotiation of definitive documents

Matters suited to financing: Criteria

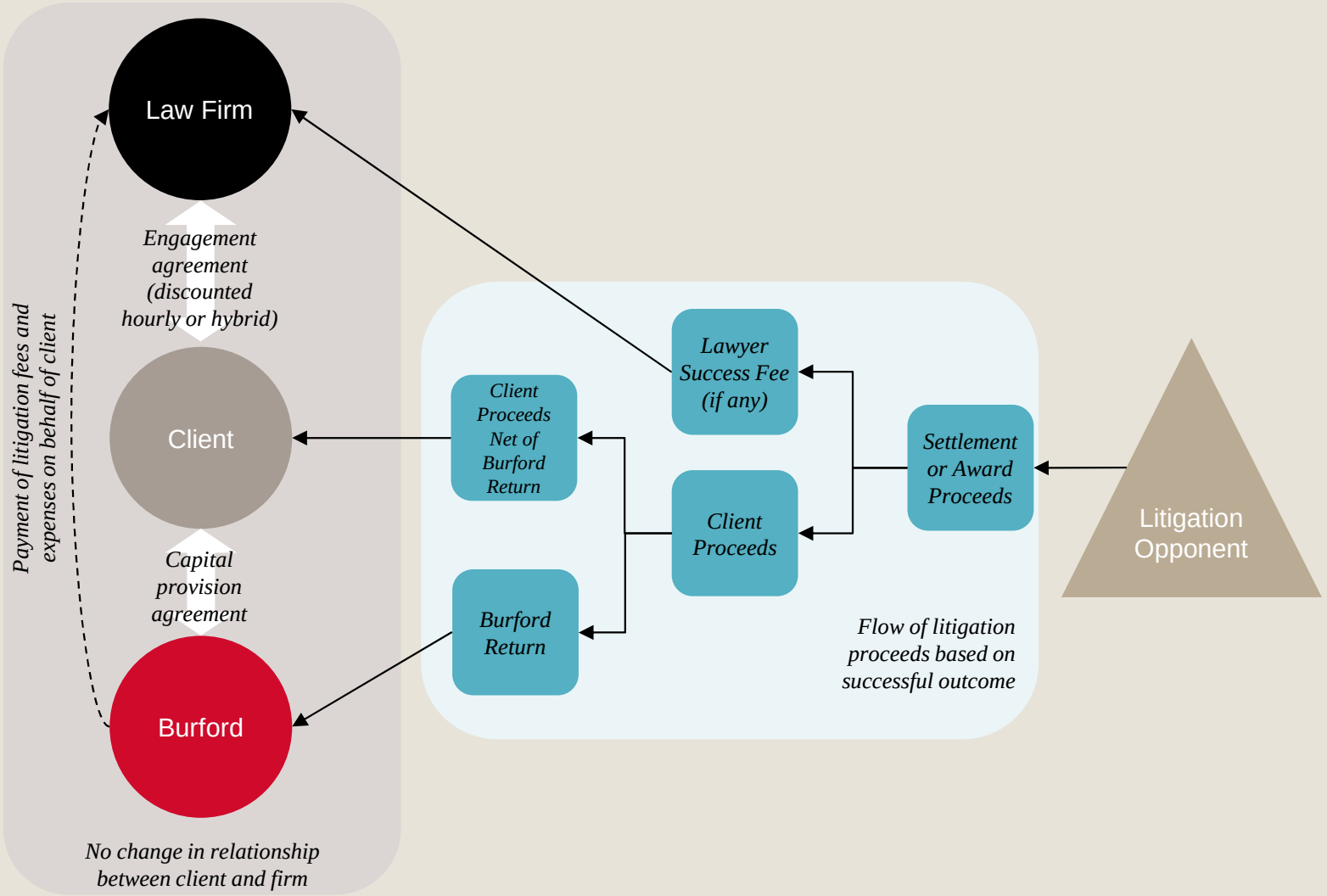
- Meritorious commercial business-to-business disputes
  - Contract
  - Fraud
  - Fiduciary duty
  - Securities
  - Antitrust
  - IP
  - International arbitration
  - Insolvency
  - Other commercial claims
- Investment need that is matched to diligence required
- Damages sufficient to support return for client, lawyers and funder

Criteria for diligencing funders

- To understand the historical track record and financial capacity of a potential provider of litigation finance, lawyers should ask
  - How much money has it made? Across how many and what kind of investments? Over what period of time?
  - How much actual cash does it have invested in comparable litigation today?
  - How much available capital does it have to invest?
  - How reliable and certain are the sources of that capital? Is it legally committed?
  - What is its investment period?
  - Who are the capital sources? (Investors' identities and the terms of the investment agreements)
  - What happens if they do not provide capital when desired?
- Given the duration of commercial litigation and arbitration, it is extremely important to identify a funder that will have sufficient capital to commit without time constraints or limitations

Basic model for litigation funding*

Litigant and funder



*Conceptual structure; does not reflect terms

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Ethical considerations

Relevant ethical topics and rulings

Ethical considerations

Overview

- Champerty
  - Largely a moot issue
  - State law considerations need to be evaluated
- Control
  - Presence of funder does not change attorney/client relationship
  - Litigation finance provider has no control over litigation strategy or settlement decisions
- Privilege
  - Parties execute NDA before any substantive discussions
  - Good case law in key jurisdictions confirming work product protection applies to funder communications and documents
- Disclosure
  - Currently not required except in a few specific instances

“Having someone else provide financing [means] we can focus on being lawyers instead of being financiers.”

– The Washington Post

Champerty, maintenance, barratry & usury

- Maintenance
  - Helping another prosecute a suit. “[T]he officious intermeddling in a suit, ‘for the purpose of stirring up litigation and strife, encouraging others to bring actions or make defenses that they have no right to make’
- Champerty
  - Maintaining a suit in return for a financial interest in the outcome
- Barratry
  - The continuing practice of maintenance or champerty is sometimes referred to as barratry
- Usury
  - Charging interest at a rate that exceeds a maximum rate provided by law for the particular category of lender involved

Champerty (1/2)

- Approaches to common-law champerty vary among states
  - As such, it is important to delve into a choice of law analysis before entering into a litigation finance agreement as some states might limit the usage of legal finance.
- Rulings in the US Federal courts and opinions from various bar associations suggest that laws concerning champerty, maintenance and barratry are outmoded and have no bearing on complex commercial litigation finance
  - "The consistent trend across the country is toward limiting, not expanding, champerty's reach." Del Webb v. Partington (9th Cir. 2011)
  - ABA Commission on Ethics 20/20 Informational Report to the House of Delegates (at 9–10): "It is unclear why the historical concerns of the common law would justify today placing special burdens on litigation funded by third parties."
  - Charge Injection Technologies, Inc. v. E.I DuPont de Nemours & Co., (Del. Super. Ct. Mar. 9, 2016): The provision of litigation finance constituted neither champerty nor maintenance. The court described the role of the litigation financier as that of a passive capital provider with no control over litigation or settlement

Champerty (2/2)

Statutory Approaches to Champerty

- A limited number states have adopted statutes that emulate common law champerty
  - New York Judiciary Law § 489 prohibits the purchase of any financial instrument or claim "with the intent and for the purpose of bringing an action or proceeding thereon"
    - Misdemeanor, also can be raised as a defense to litigation brought pursuant to a champertous purchase
    - Safe harbor where the purchase price exceeds $500,000
    - Justinian Capital SPC v WestLB (N.Y. 2016) – The safe harbor can apply in a variety of structures, so long as there is a binding and bona fide obligation to pay $500,000 or more for notes or other securities, which is satisfied by actual payment of at least $500,000 or the transfer of financial value worth at least $500,000 in exchange for the notes or other securities.
    - Trust for the Certificate Holders of the Merrill Lynch Mortgage Investors, Inc. v. Love Funding Corp., 13 N.Y.3d 190 (N.Y. 2009) – Section 489 does not apply when the purpose of an assignment is the collection of a legitimate, preexisting claim.
  - Official Code of Georgia § 13-8-2(a) explicitly names "contracts of maintenance or champerty" as contrary to public policy and thus unenforceable
  - In Illinois, 720 Ill. Comp. Stat. 5/32-11 and -12 prohibit intentional barratry and maintenance
    - Requires the champertor to "officiously intermeddle" in an action; so long as a litigant seeks out funding, a funder is unlikely to fall within this statute
  - An Alabama anti-gambling statute was used to invalidate a contract assigning part of a wrongful death suit. Wilson v. Harris, 688 So. 2d 265 (Ala. Civ. App. 1996).

Usury

- Charging interest at a rate that exceeds a maximum rate provided by law for the particular category of lender involved
- Usury only applicable where the underlying transaction constitutes a loan
- Litigation funding arrangements are not “loans” and not usurious under New York law
  - Obermayer Rebmann Maxwell & Hippel LLP v. West (W.D. Pa. 2015): Right to repayment contingent upon litigant’s success, arrangement is not a “loan” and usury inapplicable
  - Lynx Strategies v. Ferreira (N.Y. Sup. Ct. 2010): recovery contingent, not a loan and thus usury inapplicable
  - Dopp v. Yari, (D.N.J. 1996) (the majority of jurisdictions, including New York and California, permit collection of interest rates in excess of the legal rate when the collection is at risk and depends upon a contingency)
- Many states exempt commercial (as opposed to consumer) transactions from usury laws
- Investments in commercial litigation generally exceed the statutory limit for the application of usury laws

Control of counsel, strategy & settlement

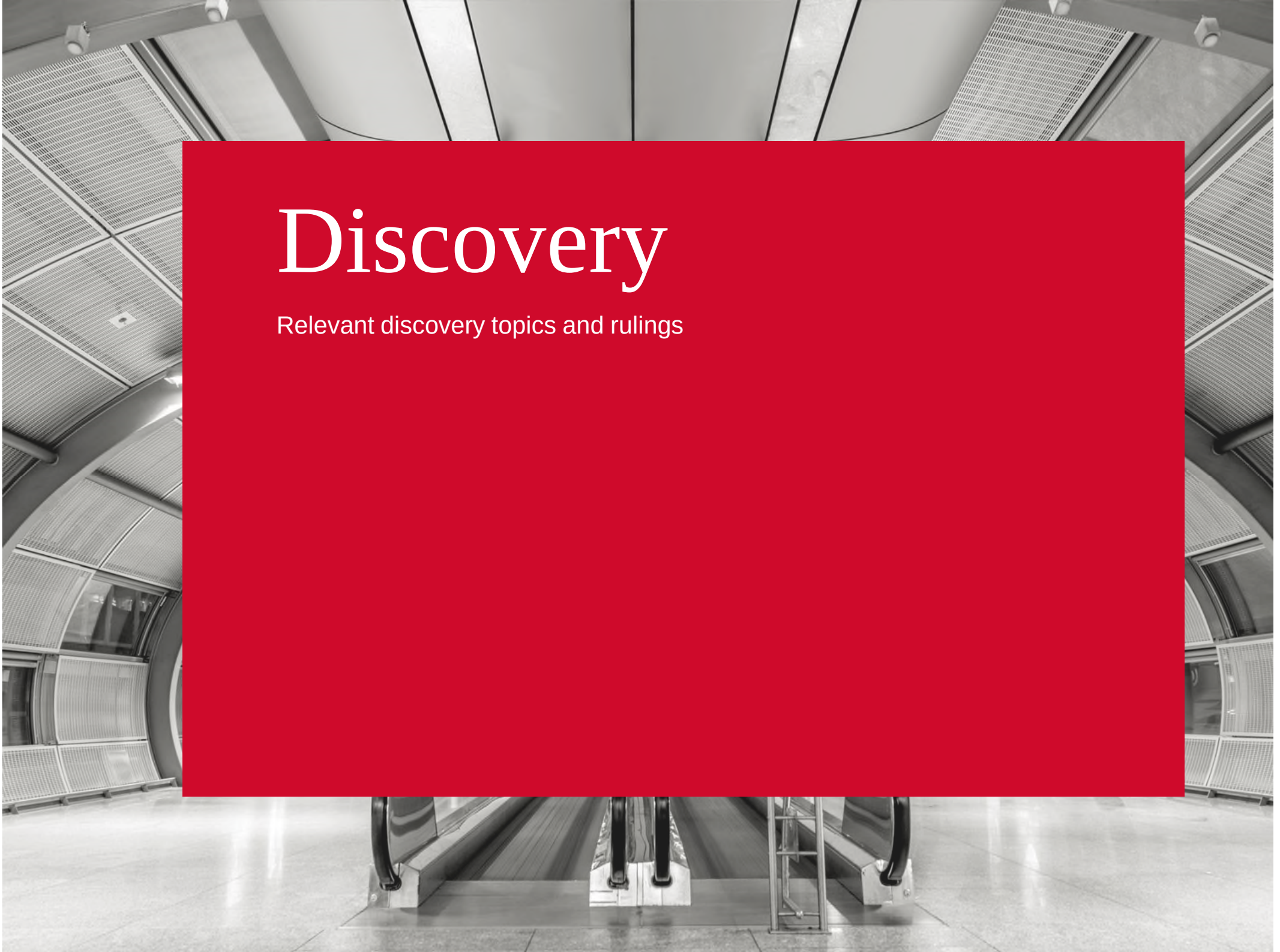
- Commercial litigation funders do not control litigation strategy or settlement
  - A client may contract with a litigation funder to restrict his/her ability to discharge counsel without funder's consent. Charge Injection Technologies, Inc. v. E.I DuPont de Nemours & Co., (Del. Super. Ct. Mar. 9, 2016)
  - However, contract between client and attorney giving the latter control over settlement is not enforceable
  - There are often multiple parties involved in settlement decisions – insurers, debt holders, minority shareholders, etc
- Client can delegate that authority to a third party according to the ABA:
  - "There would seem to be no reason, as a matter of contract law, to regard these contractual provisions as unenforceable, absent some facts establishing a defense such as duress or unconscionability."
  - "The presence of [a litigation funder] is not different in kind from the other factors that are part of virtually any decision to settle; thus, they do not present distinctive ethical issues beyond the duty of competence and the client's authority to make settlement decisions."
- Extreme case where funder has complete control over strategy and settlement, particularly when accompanied by other misconduct, may support a finding that a contract is champertous in certain states, e.g., Florida, Minnesota.

Independent judgment

- Model Rule 5.4(c): “A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services to another to direct or regulate the lawyer’s professional judgment in rendering such legal services.”
  - In a contract between the client and a funder, the client and not the funder pays the lawyer
  - Presence of a litigation funder does not change the lawyer’s duty to give client his or her best judgment
  - A delegation of the final decision on settlement to a litigation funder or other third party does not affect this duty: client always has the final decision on settlement, including the decision to delegate that authority to a third party. Charge Injection Technologies, Inc. v. E.I DuPont de Nemours & Co., (Del. Super. Ct. Mar. 9, 2016)
  - Relationship between litigation financier and client may be less intrusive than relationship with insurer, because financier typically does not have the right to decide settlement

Confidentiality

- ABA Model Rule 1.6(a): “A lawyer shall not reveal information relating to the representation of a client unless the client gives informed consent…”
- Confidential information defined more narrowly by states: “Information that is a) privileged or b) likely to be embarrassing or detrimental to the client or c) information that a client has requested be kept confidential”
- Counsel needs informed, written consent from client before disclosing confidential information to any third party, including a litigation funder
- No evidentiary privilege is created by the rule



Discovery

Relevant discovery topics and rulings

Are litigation finance agreements discoverable?

- Generally speaking, courts have held that litigation finance agreements are not discoverable so long as the Parties enter into a non-disclosure agreement that enshrines common interest protections before exchanging any information.
  - Some courts conclude that litigation finance agreements are not relevant to the litigation. *See*, *e.g.*, *MLC Intellectual Property LLC v. Micron Technology*, Inc., No. 14-cv-03657, 2019 WL 118595 (N.D. Cal. Jan. 7, 2019) (concluding that information related to litigation finance was not relevant to the litigation);
  - Other courts have concluded that litigation finance agreements are protected from disclosure by virtue of the NDA executed between the parties and common interest protections. *See*, *e.g.*, *Miller UK Ltd. v. Caterpillar, Inc.*, 17 F. Supp. 3d 711, 738 (N.D. Ill. 2014) (concluding that information shared with a litigation finance company under a NDA was protected by the work product doctrine).
  - Other courts have concluded that the information is not discoverable by virtue of the work-product doctrine and/or attorney client privilege. *See*, *e.g.*, *Devon IT, Inc. v IBM Corp*., 2012 WL 4748160 at *1 (E.D. Pa. Sept. 27, 2012) (holding that information shared with an investor under "controlled conditions" and as part of a confidentiality, common interest and non-disclosure agreement is protected by both the attorney-client privilege and the work product doctrine).

Are litigation finance agreements discoverable?

- There are a few outlier decisions to this general holding:
  - Some courts have concluded, in limited circumstances, that only the funding agreement was discoverable. *See*, *e.g.*, *Cobra Int'l, Inc. v. BCNY Int'l, Inc*., No. 05-61225-CIV, 2013 WL 11311345, at *3 (S.D. Fla. Nov. 4, 2013) (ordering production of funding agreement only).
  - Some courts have concluded that litigation finance agreements and the materials provided to a third-party financing company are discoverable when the parties fail to enter into an agreement to protect those documents from disclosure. *Acceleration Bay v. Activision Blizzard*, No. CV 16-453-RGA, 2018 WL 798731, at *2 (D. Del. Feb. 9, 2018) (holding that the work product and common interest privileges did not apply to the negotiations between a party and a litigation funder that occurred with no NDA in place and before a deal was reached and before litigation was filed).
  - As detailed below, some courts have required mandatory disclosure of the funding agreement in their standing orders.

- Best Practices Before Exchanging Information with a Funder
  - Enter into a non-disclosure agreement before sharing documents
  - Make sure you research the law of the jurisdiction the case is pending to understand discovery rules and your discovery obligations.
    - For instance, check to see if you are in a jurisdiction that requires mandatory disclosure of a funding agreement,,

Work product (1/2)

- The work product doctrine protects documents “prepared in anticipation of litigation or for trial by or for another party or its representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent).” Fed. R. Civ. P. 26(b)(3)
  - A document is protected by the work product if it “can fairly be said to have been prepared . . . because of the prospect of litigation.” 8 Charles Alan Wright et al., Federal Practice & Procedure, § 2024 (2d ed. 1994)
  - Extends to “dual purpose documents” – created for both litigation and business purposes
- The core purpose of the work product doctrine is to protect the integrity of the adversarial process – eliminate unfair advantage by prying into adversary’s strategy. See Hickman v. Taylor, 329 U.S. 495, 516 (1947)
- A party seeking financing often discloses work product to the potential financier, usually under an NDA
- Broader and harder to waive than attorney-client privilege but can be overcome by showing of necessity

Work product (2/2)

- Courts have extended the work product “umbrella” to litigation finance providers, and have protected from disclosure to adversaries work product shared with litigation financiers
- Parties obtain litigation funding to assist with litigation. Thus, the funding agreement and communications between the funder and the litigant clearly are “prepared in anticipation of litigation.”
- Every court to address the issue agrees that the work product protection applies
  - Charge Injection Technologies, Inc. v. E.I DuPont de Nemours & Co., (Del. Super. Ct. Mar. 31, 2015): Work product protection applies to payment terms in litigation funding agreements
  - Carlyle Investment Mgmt. v. Moonmouth Co., (Del. Ch. Feb. 24, 2015): Work product protection applies to documents and communications relating to third-party litigation funding
  - Miller UK Ltd. v., Caterpillar Inc., (N.D. Ill. Jan. 6, 2014): Work product protection applies to documents shared with funders, provided reasonable protective measures (such as an NDA) are in place
  - Abi Jaoudi and Azar Trading Corp. v. CIGNA Worldwide Ins. Co., (E.D. Pa. July 17, 2014): Work product protection applies to internal communication regarding litigation funding

Attorney-client privilege

- Requires that a communication made between privileged persons in confidence for the purpose of obtaining or providing legal assistance for the client remain confidential
- Applicable rules: ABA Model Rule 1.6; NY CPLR § 4503
- Sacrosanct but can be waived
  - Unlike the work-product doctrine, which is waived only when information is shared with an adversary, disclosure to any third party generally waives the attorney-client privilege, unless an exception applies
- Common interest exception may establish a non-waiver
  - Separately represented parties with a common legal interest may communicate directly with one another to advance their shared interest without waiving the attorney-client privilege.
- Frequent application of common interest: “Joint defense” agreements; Communications with insurers; M&A due diligence; Disclosure to auditors
- As a practical matter, funders may simply avoid privileged materials and instead rely on outside counsel and publicly accessible materials and information

Common interest exception to waiver of A/C privilege (1/2)

- There is a diversity of opinion on the application of the common interest exception to waiver of the attorney-client privilege in the context of litigation funding
- One view: litigation funding agreements and communications are protected by the attorney-client privilege and common interest doctrine.
  - Walker Digital, LLC v. Google Inc., (D. Del. Feb. 12, 2013): Common interest between the claimant and funder protected privileged communications Id. at *1
  - Devon IT, Inc. v. IBM Corp., (E.D. Pa. Sept. 27, 2012): “[T]he ‘common-interest’ doctrine protects communications between parties with a shared common interest in litigation strategy.” 2012 WL 4748160, at *1 n.1
  - Xerox Corp. v. Google Inc., (D. Del Aug. 1, 2011): Funder and client had an “allied, uniform, agency relationship” that qualified for common-interest protection
  - Rembrandt Techs., L.P. v. Harris Corp. (Del. Super. Ct. Feb. 12, 2009): Reached the same conclusion as to communications between a patentee and patent consultants that shared an interest in the patentee’s successful assertion of its patent claims
  - In re: Int’l Oil Trading Co., LLC, (S.D. Fla. Bankr. Apr. 28, 2016): “The information exchanged between the parties was for the limited purpose of assisting in their common cause, which was to propound litigation to collect on a claim”
- Key question is not whether both parties’ legal interests are at stake in the lawsuit, but instead whether both parties’ interests relate to the outcome of that litigation.
  - Infinite Energy, Inc. v. Econnergy Energy Co., (N.D. Fla. July 23, 2008): “The interest must, therefore, relate to litigation for this privilege to apply.”
  - Waste Mgmt., Inc. v. Int’l Surplus Lines Ins. Co., 579 N.E.2d 322, 328 (Ill. 1991) (holding that “both insurers and insureds had a common interest either in defeating or settling the claim against insureds.").
- Some courts find that common business interests in the outcome of litigation can constitute common legal interests. See, e.g., United States v. United Techs. Corp., 979 F. Supp. 108, 112 (D. Conn. 1997); SCM Corp. v. Xerox Corp., 70 F.R.D. 508, 514 (D. Conn. 1976)

Common interest exception to waiver of A/C privilege (2/2)

- Other view: No common interest protection because the funder's interest is commercial rather than legal
  - Miller UK v. Caterpillar, (N.D. Ill. Jan. 6, 2014): A shared rooting interest in the 'successful outcome of a case'…is not a common legal interest…. there was no legal planning with third party funders to insure compliance with the law, litigation was not to be averted, as it was well underway, and Miller was looking for money from prospective funders, not legal advice or litigation strategies." But while A/C privilege was waived, work product protection applied to documents shared with funders pursuant to NDA.
  - Leader Tech v. Facebook, 719 F. Supp. 2d 373 (D. Del. 2010): The court, in making numerous discovery rulings, stated that the common interest exception did not apply to privileged information that was provided to a funder. There was no common interest agreement or non-disclosure agreement in place. Ultimately materials were inadmissible.

Disclosure

- Disclosure of commercial litigation finance as practiced by Burford is neither required nor advisable, with a very few exceptions
  - In the US, the only exception at the federal level is in the Northern District of California, which since January 2017 has required the disclosure of third-party funding agreements—but only in the very specific circumstance of proposed class action lawsuits, not in single-party commercial matters
  - In the US, 49 out of 50 states do not require disclosure; the sole exception is Wisconsin
- In international arbitration, the identity of litigation finance providers may be required to be disclosed for the sole purpose of avoiding conflicts of interest
  - ICSID proposed rules (August 2018) requiring parties to declare any third-party funding as soon as a case is registered, and for arbitrators to disclose any relationship to the funder—pre-empting any conflicts of interest
- Disclosure of litigation finance isn't merited
  - Litigation finance is a private financial transaction
  - Courts have agreed that disclosure of commercial litigation finance is not merited
  - Disclosure would result in a less just, more costly and burdensome judicial system
  - Disclosure may be exploited by opponents of litigation finance (and litigation)


Questions?

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