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CONFERENCE PROCEEDINGS

# Third-Party Litigation Funding and Claim Transfer

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## Trends and Implications for the Civil Justice System

*Geoffrey McGovern • Neil Rickman • Joseph W. Doherty • Fred Kipperman  
Jamie Morikawa • Kate Giglio*

This conference was convened by the UCLA-RAND Center for Law and Public Policy. The conference and these proceedings were made possible by the generous support of Juridica Capital Management Limited, Burford Advisors LLC, Patton Boggs LLC, Oxbridge Financial Group LLC, IM Litigation Funding, and supporters of the UCLA-RAND Center for Law and Public Policy.

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## Preface

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On June 2, 2009, the UCLA-RAND Center for Law and Public Policy convened a conference in Santa Monica, California, on third-party litigation funding and claim transfer. The UCLA-RAND conference was the first ever in the United States to address this topic. The conference brought together members of academia and the nonprofit sector, stakeholders from the legal industry (including representatives from plaintiff and defense firms), and leaders from the litigation finance industry to discuss this field of finance and explore its implications for the civil justice system of the United States and other countries.

These UCLA-RAND conference proceedings summarize the key issues presented by the panelists and speakers. Supplemental materials, including briefing slides and invited papers and speeches that were written in advance and distributed at the conference, are included, unedited, in two appendixes. This volume should be of interest to participants in the legal services industry, as well as researchers and policymakers who examine the business aspects of litigation and effects of litigation finance on issues of social concern.

The conference and these proceedings were made possible by the generous support of Juridica Capital Management Limited, Burford Advisors LLC, Patton Boggs LLC, Oxbridge Financial Group LLC, IM Litigation Funding, and supporters of the UCLA-RAND Center for Law and Public Policy.

The mission of the UCLA-RAND Center for Law and Public Policy is to inform legal and public policymakers with innovative legal scholarship grounded in multidisciplinary empirical analysis. The center fosters collaborative research, holds conferences, and trains law students in the Empirical Legal Scholars program. It is the first center of its kind to create a partnership between a law school and a major nonprofit research institute.

Founded in 1949, the University of California, Los Angeles, School of Law is the youngest major law school in the nation and has established a tradition of innovation in its approach to teaching, research, and scholarship.

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## Introduction

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Litigation can be expensive and risky. Some people seeking justice may be unable to pursue or defend a claim because they cannot afford the costs or find attorneys willing to assume the risks. Furthermore, because of real and perceived restrictions on the transfer of claims, claim-holders have limited opportunities to hedge litigation risk. Third-party litigation funding, still in its infancy in the United States, has the potential to equalize the bargaining power of litigants in the civil justice system and provide new risk reallocation products to businesses. In essence, third-party litigation funding is a novel method of litigation risk allocation and a way to bring market forces to bear on the supply of money used to finance legal claims. Supporters of the approach believe that these new arrangements can increase access to justice and lower the direct, or transaction, costs of litigation. Opponents believe that this new approach will unnecessarily increase the aggregate amount of litigation and promote profiting from another's harm.

Currently, there are three distinct, active segments of third-party funding for plaintiffs in the United States. First, many companies provide *nonrecourse loans* to individual plaintiffs, often plaintiffs in tort suits. Several lenders in this segment, which is sometimes referred to as the “cash advance” business, are members of a trade association called the American Legal Finance Association. Second, some companies provide *loans* to plaintiffs' law firms—loans that are secured by all the assets of the borrowing firm (e.g., its portfolios of lawsuits, real estate, office furniture). Third, some companies *invest* in individual commercial claims brought by corporate plaintiffs in areas such as intellectual property, antitrust, and contracts. The term *investment* is used fairly often to distinguish this activity from “loans” characterizing the other two segments and to indicate that the funder's (or investor's) return includes a proportion of the eventual recovery in the lawsuit.<sup>1</sup>

The policy questions surrounding third-party financing were the focus of a conference convened by the UCLA-RAND Center for Law and Public Policy on June 2, 2009. The conference, titled “Third-Party Litigation Funding and Claim Transfer: Trends and Implications for the Civil Justice System,” brought together lawyers, business leaders, academics, and members of the nonprofit community for a discussion of litigation financing and the effects that new financing arrangements might have on the legal-services industry in the United States.

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<sup>1</sup> Much of the discussion at the conference did not distinguish among the segments, but some participants did so explicitly or implicitly (e.g., by raising issues that are not relevant to all segments). In these proceedings, we distinguish among the segments only if the speaker did so or when the distinction is crucial to avoiding misunderstanding.

*Third-party financing*, as the term is typically used, is fairly new in the United States.<sup>2</sup> However, it is gaining ground in other common-law countries, most notably in Australia (whose third-party litigation finance industry has matured over two decades) and England and Wales (where the decade-old market has rapidly developed in the last three to four years). In these countries, a small but growing legal-finance industry is developing.

The UCLA-RAND conference was the first symposium in the United States to focus specifically on the third-party litigation finance industry and its implications for the U.S. legal-services industry and various other outcomes of social concern. The conference objectives were broad, and the focus was largely theoretical. To begin to examine how third-party financing is developing in the United States, the conference generally addressed the following issues:

- How can the current state of U.S. third-party litigation finance be described?
- What developments may take place in the near future?
- What effects might third-party finance have on dispute resolution, and are these effects desirable?
- What possible regulatory responses can the United States expect?

These proceedings highlight key insights from the conference. They begin with a synopsis of the prepared talks given by the first two invited speakers, each providing a solid introduction to the central issues surrounding third-party litigation finance in the United States. The following sections outline the three conference sessions' topics and themes, presenting a summary of the remarks prepared by the panelists. The first panel furnished a description of the traditional litigation finance landscape in the United States, highlighting the roles of insurers and contingency-fee lawyers, two well-established groups of litigation financiers. The second session included a more detailed discussion of the operation of present-day third-party funding practices in the United States and put forth some predicted challenges awaiting novel funding arrangements. The third session covered some of the regulatory and ethical issues that may be raised by (or could hinder the development of) third-party financing. The proceedings conclude with an outline of the closing roundtable discussion, which provided an open and lively venue for conversation between panelists and the audience, and some summary remarks. Two appendixes provide supplementary materials. The conference agenda, a list of participants, presenter biographies, and an overview of the goals of the conference are included, unedited, in Appendix A. Appendix B contains the complete text of the keynote address and presenters' briefing slides, also unedited.

Although a certain amount of researcher attention has been paid to this topic, until this conference, third-party litigation funding in the United States had received little sustained reflection. The conference was organized to provide substantial introduction to the topic and to describe the more complicated matters that have the potential to reshape the ethical and financial foundations of U.S. law. The conference also offered the chance to reflect on the complex interface that is developing between capital markets and the contemporary legal system.

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<sup>2</sup> Common practices, such as claim transfer in bankruptcy, contingency-fee contracts for provision of legal services, and payment of the litigation defense costs of policyholders by their insurers, might also be described as "third-party litigation financing."

## Opening Remarks and Framing the Central Issues

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The purpose of the opening remarks was to outline the role that litigation serves in society, how litigation is typically financed under the current system, and how the system of financing litigation might impede or advance some social goals. Two speakers presented opening comments before the first panel session began. Lynn LoPucki, the first speaker, outlined some of the fundamental purposes of and challenges facing the current litigation system. Selwyn Seidel then identified some key players involved in third-party litigation, their roles, and some of the primary products offered through third-party funding options in the United States and abroad. The full text of Seidel's prepared paper is included in Appendix B.

### **Litigation's Purpose, Shortcomings, and the Desirability of More Litigation**

*Summary of Remarks by Lynn LoPucki, Security Pacific Bank Professor of Law, UCLA School of Law*

Litigation serves several social functions. The most immediate benefit of litigation is its ability to compensate victims for harms done to them. Litigation makes monetary damages available for, among other things, victims' medical bills, contract breaches, and patent and copyright infringement. Litigation also prevents the externalization of costs. Externalities affect people who are not parties to a transaction. Consider a manufacturer of a product that causes broader societal harms, such as pollution. By allowing the victims to sue, the litigation system may impose those otherwise-externalized social costs to the manufacturer, in turn causing the manufacturer to include those costs in the price of its product. The increased price reflects a transfer of the social costs back into the transaction, instead of onto society at large. More broadly, litigation corrects injustice, provides a pattern of outcomes that guide future conduct, resolves disputes nonviolently, and deters future misconduct. Holding people liable for their actions causes potential future defendants to think twice about their behavior and avoid harmful acts.

Yet, the litigation system does not serve these social functions flawlessly. As suggested by the example of medical doctors practicing defensively to avoid litigation, the litigation system may overdeter future risky, yet socially desirable, behavior. Similarly, the system underdeters future misconduct when too few cases are brought. For example, domestic abuse is chronically underreported, and private claims arising from such abuse are especially rare. Injured people may be reluctant to bring claims, perhaps for reasons of cost, privacy, or the length of time required for resolution. In fact, most people who have valid legal claims fail to bring them.

### **Litigation Costs Influence Behavior**

All the aforementioned social functions of litigation run into the problem of cost. Lawsuits are an exceptionally expensive way of compensating victims or deterring socially undesirable behavior. Because the process is so expensive, many with valid claims forgo litigation completely and thus weaken litigation's deterrent effect.

Third-party approaches to financing litigation can change the way litigation costs affect litigant behavior. The availability of outside funding may encourage more parties to pursue their claims. Litigation financing, theoretically, could "level the playing field" by attenuating or eliminating resource disparities between plaintiffs and defendants. It could provide access to the courts for those who could otherwise not afford protracted litigation. This could reduce the problem of unfiled claims. (Only if all valid claims were filed and resolved would the deterrent effect of the litigation system be realized.)

But the consequences may not be so desirable. Financing may not flow to those litigants who cannot afford to litigate, but instead to those who appear at the outset to have the most meritorious cases. In this scenario, financing would not so much level the playing field as it would ensure the success of those who appear strongest going in. Even meritorious cases may not receive funding if their prospects are difficult to evaluate.

Another approach to litigation financing, claim transfer, presents additional difficulties and raises ethical concerns. To illustrate, an injured worker with a \$10 million claim cannot afford to risk an uncertain trial and instead sells his claim for \$1 million to a litigation financing company. The worker will recover a sum certain and transfer the risk to the financing company, which likely is better equipped to incur the risk. This arrangement preserves the likelihood that the valid claim will go to trial and render justice to the defendant. But the less-than-full compensation given to the victim raises ethical issues. A trial might show that the case was meritorious and the victim should have received \$10 million. Alternatively, it might show that the plaintiff was not entitled to anything at all. Either way, the original plaintiff's \$1 million recovery was not the right result.

### **Conclusion**

Third-party funding options raise a variety of difficult questions about the current litigation system. If third-party funding increases aggregate litigation, increases particular kinds of litigation, or systematically alters the outcomes of litigation, those changes will have to be examined and justified.

### **Stakeholders and Products in Third-Party Funding Arrangements**

*Summary of Remarks by Selwyn Seidel, Partner, Burford Advisors*

At the core of the legal industry are the claimants. Claimants, those seeking to recover monetary damages through a lawsuit, drive civil suits and may benefit significantly from third-party financing arrangements because these options offer new sources of funding to support court action. Claimants come from all over the world and represent a broad spectrum of legal claims. Yet, third-party finance researchers know little about these claimants' use of and potential need for access to outside funds. There are no statistics to aid assessments of the most needy practice

areas. Because the current situation is like “flying without instruments in the night,” an empirical research program is needed.

### **Financers Must Balance Risk and Reward**

Currently, seven independent institutions offer financial services to claimants; these institutions are independent insofar as they do not provide actual legal representation for the claimants. Many of them are private companies, so data are not readily available. Each institution creates its own set of preferences to guide decisions about where to allocate capital, just like any other financial services firm. Although these financers collectively provide three types of funding (investment in claims, recourse loans, and nonrecourse loans), claim investments receive the most attention. For each approach, the firm management decides which claims are worthy of financing by evaluating the size of a candidate claim, the type of claim involved, and the likelihood of settlement within a given time frame. As with any such financial industry, the financing institutions are balancing risk and reward across a portfolio of business opportunities.

### **Contingency Law Firms May Play Different Roles**

Within the funding arena, contingency law firms are sometimes competitors, and sometimes collaborators, relative to the institutional financers. They compete by investing their firms’ capital in place of outside funds. This is the standard practice in the United States, but it is rare in jurisdictions that do not allow for contingency-fee contracts. These firms could, however, cooperate with institutional financers, allowing for a division and specialization of labor between capital and legal-service providers. This is just one more dimension that will develop in response to market and regulatory forces in the future.

### **Insurance Companies Still Have an Undefined Role**

Insurance companies also populate the field, although the future role of insurers in third-party financing arrangements remains incompletely defined. Whether insurance companies will be collaborators or competitors will depend on the circumstances of the claim, the jurisdiction, and the priorities of the insurance firm.

### **Key Products**

The products being offered by third-party financers are almost as varied as the claims they fund. Under what the speaker termed “the standard arrangement,” the financier funds the claim and awaits the outcome. Here, the financing firm pays the direct costs of litigation, such as attorneys’ fees, court costs, expert witness fees, and document processing costs, in exchange for a share in any future recovery. This share and all other aspects of the relationships among the claimant, the financier, and the lawyer are specified in contract. Two other funding approaches do not invest in the claim but provide loans either to plaintiffs or to their attorneys. These loans may be secured by other assets or may require repayment of principal and interest only if the final recovery suffices to cover these debts. Beyond these common contracts, however, there are agreements for collateralization for personal expenses or for commercial needs. There is also an emerging interest in funding defendants (although this segment of the market is not as developed).





## Session One: The Current Landscape—Funding Claims in the United States

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This session focused on the wide variety of funding options currently available in commercial and individual litigation, on both the plaintiff and defense sides. Insurers and attorneys are a relatively standard source of third-party finance, but developments—including a move toward complex litigation—are creating opportunities for new sources of capital to help fund cases in the United States and Europe. Herbert Kritzer, the first panelist, gave a presentation on fee regimes and how attorneys are compensated for their services. Neil Rickman presented views of litigation finance as practiced in Europe. He emphasized the role played by insurers in European litigation funding. James Tyrrell discussed the various ways that lawyers in the United States are financing litigation in the absence of third-party resources.

### Fee Regimes

*Summary of Remarks by Herbert Kritzer, Professor, William Mitchell Law School*

The primary concern driving this conference was how lawyers are and can be compensated for their services. Legal fees underlie the incentives faced by legal disputants and their actions. Fees ultimately influence all work that is done; the decisions made by lawyers and clients and the desired outcomes directly affect the costs associated with various legal strategies.

#### “Fee Regimes” Defined

The different ways in which legal services can be provided and paid for can be classified as “fee regimes.” Simply put, a fee regime is the structure of attorney compensation for contentious work, including litigation, arbitration, administrative adjudication, or settlement of claims in the absence of third-party funding. Fee regimes include who pays, how fees are calculated, and how fees are regulated. There is a range of potential combinations. For example, legal rules may stipulate that each party pays his or her own fee or that the loser pays the winner’s incurred expenses. In each case, the fee may be flat, hourly, or contingent. Regulation can be performed by the courts, by well-informed client auditing, or by reference to accepted norms and standards.

#### Allocating Risk Through Fee Regimes

The variety of available fee regimes could be used to allocate risk to the most appropriate risk bearers. There are many kinds of litigation, and each poses different risks to the involved parties. Individual claims have a clearly identified plaintiff who can choose to bear all of the risk by financing a lawsuit out of pocket, while large, complex class-action cases can potentially

include thousands of plaintiffs, none of whom may desire to finance even their individual claim because recovery, in the disaggregate, is too meager. Contingency fees may allocate the risks of litigation to more appropriate risk bearers. Of course, this does not always happen, but patterns that are consistent with it can be observed.

### **The Future of Third-Party Litigation Financing**

In the context of this symposium, the variety of currently used fee and financing arrangements suggests that third-party litigation finance is most likely to flourish if a market gap exists. Third-party litigation finance may thrive if it provides a more attractive and efficient allocation of risk than currently available fee and financing arrangements.

### **Insurance and Litigation Funding**

*Summary of Remarks by Neil Rickman, Founding Director, Institute for Civil Justice, RAND Europe*

Insurance plays a high-profile role in litigation. In many European jurisdictions, legal insurance indemnifies a litigant for legal expenses incurred while pursuing or defending a claim. It is popular to purchase “before-the-event” insurance that covers legal expenses associated with going to trial, even before a specific claim arises. There is growing interest in policies purchased “after the event.” (In this context, the “event” is the advancement of a legal claim.) This type of policy protects the litigant from incurring liability for the opponent’s legal expenses in the event of a failed legal claim. Many European jurisdictions operate under a loser-pays principle (often called the “English Rule”) in which the losing party must pay the winning party’s legal expenses in addition to any compensation that might be awarded.

### **The Role of Insurance in the United States Involves the Subrogation of Claims**

“Before-the-event” and “after-the-event” legal insurance policies are not common in the United States, but this may change as third-party financing becomes increasingly popular. Insurance in the United States commonly involves the subrogation of claims. This is also prevalent in Europe. In this case, the insurer pays on a claim to its policyholder but then sues for recovery from a third actor who caused the damage covered under the policy. For example, an insurance company pays its policyholder after an auto accident caused by a negligent driver. The insurer will then sue the negligent driver to recover the money it paid out. In the absence of the insurance policy, the policyholder likely would have sued the negligent driver. But by virtue of the insurer’s relationship to the insured, the insurer has the right to recover damages. This is a form of claim transfer, although it is not commonly referred to as such, and it has the potential to cause problems because the policyholder now has no financial interest in the case. However, uninsured losses and deductibles, the insured’s concern for his or her loss record, and, ultimately, a subpoena, may mitigate this problem.

### **Possible Roles for U.S. Insurers**

Insurers may play both complementary and competing roles in third-party litigation financing. After-the-event insurance in cost-shifting jurisdictions already adds a third party into the mix, but this type of insurance is generally available in only some European jurisdictions. An

insurer may join a pool of other investors with interests in financing a claim from the start, thus becoming an investor in a claim and not an insurer of a claim. But insurance may compete with more direct forms of litigation financing; after-the-event insurance may dissuade litigants from seeking third-party sources of funding altogether.

### **The Future of Insurers as U.S. Litigation Financers**

Although the idea of insurers as litigation financers differs from most other models presented at the symposium, insurance may provide a sensible model for study—a point strengthened by its European relevance. Insurers may provide a bridge between the role of fee regimes and third-party financing mechanisms.

## **Lawyer Investments in Claims**

*Summary of Remarks by James E. Tyrrell, Jr., Regional Managing Partner, Patton Boggs LLP*

The contingency fee is common in the United States, but it is rare or proscribed in other countries. Under a contingency-fee arrangement, a lawyer finances a claim by putting his or her time and expenses on the line. Often, an attorney on contingency will take a case without payment for services until and unless the plaintiff wins. After victory, the attorney will take a percentage of the recovery. This arrangement provides access to capital in the form of the lawyer's time and resources while maintaining harmony in lawyer and client interests. In this arrangement, the lawyer provides high-quality service because his or her income depends on performance.

### **Lack of Sufficient Funds Can Be Alleviated Through Various Options**

On occasion, a lawyer does not have sufficient funds to finance the claim, as in expensive cases requiring, for example, expert witnesses, expert reports, or scientific studies. One option in such a scenario is that the would-be plaintiff cannot pursue the claim. Alternatively, wealthier law firms may step in to provide the necessary funds to the plaintiff in return for a share of the damages. The result of this type of arrangement is a law firm with an equity stake. This situation can be described as “classic litigation,” in which an insurance-backed defendant and a plaintiff backed by a contingency-fee lawyer and a litigation fund square off in court.

### **“Banker-Lawyers” Are Increasingly Relevant in the Current Litigation Environment**

In today's complex litigation environment, “banker-lawyers” frequently sponsor multiple insurance-backed defendants against a number of class-action plaintiffs. Banker-lawyers are capable of advancing capital and bearing the significant risk associated with a contingency fee. Banker-lawyers frequently turn to other suppliers of capital who are willing to enter into a joint venture to support litigation.

Some high-profile cases demonstrate the different arrangements that have been used. Some national alcohol litigation involved a plaintiff's firm using assets from asbestos litigation to fund litigation against alcohol manufacturers. The Agent Orange cases, in contrast, required an informal joint venture of several firms that pooled their resources. More formal joint ventures have been created in response to 9/11 litigation.

### **The Growing Need to Fund Plaintiffs Provides New Opportunities**

The abundance of funds now available to plaintiffs may have “tipped the funding scales” toward plaintiffs, creating an imbalance of resources. Of course, there is some concern about access to justice, but this situation has the potential to create opportunities for financiers on the defendant side, as well as banker-lawyers and joint venture funders financing defendants.

There are several possibilities for such “defendant funding.” Incentives could be provided to defendants’ attorneys by offering a fraction of the value earned by defeating a summary judgment motion, or investors could be offered a fraction of sales revenue or profits if a block injunction is defeated.

## Session Two: Litigation Markets, Participants, and the Structure of Claim Investments

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Claim transfer, or the sale of the rights to recovery to an outside investor, is emerging as one of the most influential trends in civil justice, and it is shaping how civil litigation is funded in the United States and abroad. The second session focused on the structure and scope of the current U.S. market for claim transfers, as well as challenges facing the further development of claim transfer activities. Tim Scrantom described the types of claim transfers currently available and the economic and structural reasons for the claim market's current form. Jonathan Molot presented ideas about risk allocation and assessment, highlighting two significant obstacles hindering the development of this new industry.

### Sources and Structures of Claim Investments

*Summary of Remarks by Timothy D. Scrantom, President, Juridica Capital Management (U.S.), Inc.*

The United States is the largest market for claim transfers in the world, and it is one in which claim transfers occur on a regular basis. Intellectual property litigation and bankruptcy claim transfers are so commonplace that few would think to object to them based on the funding source. The dominant position of the U.S. legal market makes further developments in claim transfer likely.

The dominance of the U.S. market developed for a number of structural reasons. For example, the sheer size of the U.S. legal industry draws third-party investors seeking new opportunities for financial returns. Likewise, the amount and value of litigation makes the U.S. market an obvious target of interest. Perhaps more strategically, the ingrained understanding of contingency-fee structures, which are essentially a variant of claim transfer to law firms, makes third-party financing seem less extreme, in theory, in the United States than in jurisdictions that do not allow lawyers to finance the claims of their clients.

Why is the U.S. legal industry so large and attractive to claim investors? Some of the influences include the role of the jury trial in civil cases and the substantial awards that can be recovered. In some cases, special damages, such as treble and punitive damages, make claims a potentially profitable asset. Likewise, special litigation regimes (such as class actions) allow the aggregation of potentially thousands of low-value claims and present another opportunity to create value.

All of these elements add up to an "open market" for the transfer of claims. In fact, despite some suggestions that Europe first developed third-party financing, certain types of claim transfers regularly take place in the United States. Third-party financing arrangements can result from not only contingency-fee arrangements but also bankruptcy cases and the

transfer of intellectual property claims. Patent claims are transferable under federal law. As a result, patent claim transfer and acquisition is a multibillion-dollar industry. Additionally, there is an accepted U.S. market for bankruptcy claim transfers. Creditors with preexisting rights have purchased claims out of bankruptcy without running afoul of champerty prohibitions that are designed to prevent ethical breaches. Other forays into claim transfer include a small but influential retail market for personal injury claim monetization. Approximately 40 firms are involved in monetizing parts of claims prior to recovery, sometimes providing capital for living expenses in addition to litigation-related costs. Large U.S. law firms are beginning to recognize the value of nontraditional capital sources, partly as a result of client demand for fixed fees and risk sharing. It seems that claim transfer is already big business in the United States.

### **How Does and Can the Claim Marketplace Generate Capital?**

The size of the U.S. market draws interest from claim investors. But what form will these investments take, and how much capital may flow into litigation? It is estimated that, in the past five years, the capital flowing into the claim marketplace was around \$5 billion. Most of this revenue was gained through intellectual property claims, and this number is exclusive of contingency fees.

The form of financing will be driven, in part, by the demand for claim investments. Some clients are demanding new ways to finance their cases, spurring interest in novel financing arrangements. Other industry participants are looking to hedge against the risk of pursuing an asset that has speculative value. On rare occasions, companies sell and securitize claims as nontraditional assets. As with most investments, standard factors influence investment in legal claims, such as claimholder and investor needs, control issues, legal restrictions and remedies, security of loans (recourse/nonrecourse), and tax implications.

### **The Types of Products Currently Offered Are Extensive and Can Be Tailored**

The ways in which claim investments are structured vary greatly. Some financiers directly purchase interest in a claim, often in commercial litigation. Other financing takes the form of loans. A nonrecourse loan would be, essentially, a no-win, no-fee arrangement: The financiers would grant a loan to a claimant for litigation expenses (and perhaps living expenses) in exchange for a payment if there is a recovery. No recourse to other secured assets would be available to the financier. Some companies also lend to firms, with the loans secured by the firm's assets. Insurance arrangements, derivatives, and hybrid models can be used and are currently employed in third-party funding. The variety is extensive and allows funding arrangements to be tailored to the special needs of the claim and claimant.

### **Litigation Markets and Litigation Accuracy**

*Summary of Remarks by Jonathan Molot, Professor, Georgetown Law School*

The obstacles facing claim transfer can be either technical or ethical. Regardless, third-party financing might be an innovation that leads to more accurate settlements and, thus, a more efficient legal system.

## Two Obstacles to Open-Market Litigation Financing

The first core obstacle to third-party litigation financing in the United States is uncertainty in pricing risk. Pricing is a particularly significant obstacle because lawyers price claims in a way that is not as sophisticated as that used in some existing financial risk models. Litigation risk assessment depends on a number of variables that interact and increase uncertainty. Facts, the jury pool, the incentives to settle, the opposing counsel's skill, the presiding judge, and current law are all factors influencing uncertainty.

Complexity in risk modeling is not a unique feature of litigation risk. Calculating default risk for corporate bonds is just as complex; macroeconomic factors, currency fluctuations, interest rates, and micro-level factors are just a few of the variables currently used in financial risk assessments, particularly in the credit default swap market. However, it is not the case that there is no market in litigation claims *because* claims are difficult to price; instead, claims are difficult to price because there is no market.

In theory, then, the obstacle of accurate risk pricing can be overcome. Indeed, this happens frequently during settlements, when attorneys weigh the probability of trial success against the value of a settlement offer.

The second core obstacle is stigma, which encompasses all restrictions needed to take advantage of outside funding. Champerty and maintenance doctrines, as well as restrictions on fee sharing, are examples of this. Such restrictions leave mainstream lawyers on the sidelines. If these prohibitions could be reformed, then there would be more potential for growth. It should not be difficult to reduce or eliminate the stigma: If the goal is to shape litigation outcomes to achieve social goals, rebalancing access to litigation funding can be effective.

## The Role of Accurate Settlements

Since the majority of cases settle, accuracy in settlement decisions is enormously important. The goal is for settlement outcomes to track trial outcomes. If, however, parties are settling based on cost or risk-tolerance factors and not on the merit of the claim, the system breaks down. Defendants get off too easily or plaintiffs reap excessive gains.

These inefficient settlements are a result of parties' risk preferences. For example, when a lawsuit sets a one-time plaintiff against a repeat defendant, the risk imbalance favors the defendant, because one-time players cannot spread risk over several rounds of litigation. Thus, the plaintiff has the incentive to settle at a lower level of recovery than would otherwise be the case. On the other hand, in mass consumer class actions, strong plaintiffs are more risk tolerant than defendants facing huge one-time judgments. Hence, settlements can be a function of imbalances in bargaining power and not about the merits of a case.

The disparity in settlements is just as much a market failure as it is a failure of civil procedure. As such, introducing a risk-neutral repeat player on the side of the risk-averse party can remedy the imbalance. It would promote accurate deterrence by ensuring, for example, that defendants pay amounts closer to the mean expected damages for similar claims that have been resolved through trial.





## Session Three: Rules, Regulations, and Ethical Considerations of Third-Party Funding

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Legal systems in the United States and abroad are guided by a complex set of rules, regulations, and professional ethical obligations. This session addressed the interplay between professional codes and ethical principles on the one hand and third-party litigation funding on the other. With an increased number of outside players involved in an alternatively funded case, some of whom are not governed by these rules or obligations, how are issues of confidentiality and independent professional judgment affected? Does the absence of statutory or case law delineating responsibilities (disclosure and consent) and protections (attorney-client privilege) distort the reaction of clients and, similarly, encourage aggressive client advocacy? And finally, under what circumstances does third-party funding level the playing field by allowing meritorious cases to go forward? The end of this line of inquiry returns to Lynn LoPucki's opening remarks. While third-party lending institutions can help ensure that financial pressures do not interfere with the fair and just disposition of an underfunded plaintiff's lawsuit, we must also be mindful of its capability to alter the integrity, fairness, and truthfulness of the litigation system.

### Professional Ethical Issues in Third-Party Litigation Financing

*Summary of Remarks by Nathan M. Crystal, Distinguished Visiting Professor of Law, Charleston Law School*

Third-party financing may occur within one of four types of legal relationship structures. Each of these structures produces its own ethical concerns, which may pose barriers to third-party financing.

#### Four Types of Legal Relationships

Four "transaction structures," or ways in which third-party financing of litigation occurs, can facilitate an examination of how the ethical issues of confidentiality, fee splitting, and independent professional judgment can be resolved.

**Outright Purchase of a Cause of Action.** The first structure is the purchase of the cause of action or the assignment of the proceeds of any judgment or settlement. In this case, the financing entity would buy the claim, or purchase the rights to the proceeds of the claim, from the plaintiff. Local laws regulating claim transfers will influence whether this is feasible. If transfers are prohibited, then it may be possible to structure the transaction as an assignment of the proceeds rather than as a purchase of the claim itself.

**Plaintiff Loan: Coverage and Terms.** The second type of structure is a loan to the plaintiff for litigation expenses. Expert witness fees, document examination, and a portion of the

legal fees if the fee regime was not a pure contingency fee are some examples of these expenses. There is no reason that such a loan would be limited to the costs of litigation; essentially, it could also include funds for general purposes as well as litigation expenses. Loan terms would thus be negotiated between the parties based on an analysis of the degree of risk involved and the degree of risk to be assumed by the financing party. These loans may be recourse or nonrecourse.

**Law Firm Loan: Coverage and Terms.** The third type of transaction structure is a loan to the law firm, rather than to the plaintiff, for the expenses of the case. While all the terms of the loan, such as the rate, recourse, and its use, are subject to negotiation, the loan itself raises some additional ethical issues of disclosure and client consent. The law firm would need to disclose the loan terms to the client and obtain client consent to pursue this line of financing.

**Co-Counsel Relationships.** A fourth type of transaction structure is a co-counsel relationship between a law firm funded by the financing entity and the law firm that is handling the case. This is an option if the local law is hostile to a direct purchase of the claim or if a loan is undesirable for any reason. It involves the banker-lawyers, discussed earlier by James Tyrrell, working as co-counsel on the case, even though the real command and control remains with the plaintiff's firm.

While these four structures raise legal questions of champerty, maintenance, usury, and public policy restrictions, there are also serious ethical issues of confidentiality, fee splitting with nonlawyers, and interference with independent professional judgment.

### Ethical Concerns

**Confidentiality in Legal Relationships.** Concerns about confidentiality—distinct from the attorney-client privilege or the work-product doctrine—are raised when a lawyer must disclose information to the financing agent. This information must be disclosed initially to allow the financing entity to evaluate the case, and it will be required during the case to monitor and protect the financier's involvement. The client, in order to obtain financing, would need to be willing to disclose this information and should obtain counsel about the risks associated with such disclosure. There is no ethical problem from the lawyer's perspective if a properly counseled client decides to reveal information to a third-party financing entity.

However, disclosure of information does raise questions about the attorney-client privilege and the work-product doctrine. For example, is the attorney-client privilege lost when a lawyer reveals client information to a financing entity? Local jurisdictions' requirements for the evidentiary privileges will govern, of course, but provisions of the *Restatement of the Law Governing Lawyers* also demonstrate the problem.

Under the *Restatement*, there are certain requirements for the privilege to apply; primarily, there must be communication between privileged persons in confidence for the purpose of obtaining or providing legal assistance for the client. Whether the attorney-client privilege applies to a third-party financing arrangement depends on (1) whether the communication with the financing entity is between privileged persons and (2) whether communication with the financing entity constitutes obtaining or providing legal assistance.

Resolving these two problems is no easy task. While the litigation may not be able to proceed without financing and thus may constitute the provision of legal assistance, it is difficult to equate a financing relationship with the attorney-client relationship. Structuring the relationship in various particular ways might protect the privilege. That is, attorneys for the financing entity could be designated as agents of the client for the purpose of receiving

confidential information and evaluating the client's claim, like a second opinion. Another possible structure is an attorney-client relationship between the attorney for the financing entity and the client for the purpose of case evaluation. Here, the disclosure would be in the context of providing legal advice. This raises conflict-of-interest questions, because the attorney for the financing entity would also be the attorney for the client. This conflict can be disclosed and consented to, but there would need to be adequate disclosure and consent.

With regard to the work-product doctrine, the standard test is whether the material was obtained or prepared in anticipation of litigation. If it is work-product material, another party may obtain the information only if it shows a substantial need for the information and that it is unable to obtain the information without undue burden. The work-product doctrine would clearly apply to the type of information conveyed to the financing entity; all of the relevant information is prepared in anticipation of litigation. It is difficult to see how an opposing party could claim a substantial need for the information or that it could not obtain the information without substantial burden or expense.

There remains the question of whether disclosure to the financing entity amounts to a waiver of the work-product protection. Under the *Restatement of the Law Governing Lawyers*, work-product immunity is waived if the client, the client's lawyer, or another agent of the client discloses the material to third persons in circumstances in which there is a significant likelihood that an adversary or potential adversary would obtain it. If the material is disclosed to a financing entity under nondisclosure agreements, adequate steps could be taken to prevent the information from being disclosed to an adversary.

Along with legal steps taken to protect the confidentiality of information, there are also practical ones to consider. Measures such as confidentiality agreements, court orders forbidding disclosure, return of the documents to the client after review, and keeping the material offshore may make it possible to further establish confidentiality.

**Fee Splitting.** Fee splitting is also an ethical concern. The general rule in almost all jurisdictions of the United States propounds that lawyers may not divide fees with nonlawyers. If the transaction structure involves a purchase of cause of action or of the proceeds, or if it involves a loan to the client, fee splitting would not be a problem. In a co-counsel arrangement, there is no fee-splitting problem because the parties are lawyers. The fee-splitting problem could arise in the context of a loan to the law firm. The source of the payments on the loan, legal fees, cannot be the test for whether fee splitting occurs because fees are used to pay salaries and other expenses to nonlawyers, not just the loans. A number of ethics opinions and academic articles contend that the borrowing of money by firms and payment of interest do not amount to improper fee splitting.

If the source of the payment is not an issue, the next question is whether the practice undermines any of the policies on which fee-splitting rules are based. The prohibition against fee splitting protects the lawyer's professional independent judgment, specifically in preventing nonlawyer control over lawyer services. To protect the lawyer's independent judgment, the financing agreement should contain provisions advocating that the lawyer and client retain the right to make all decisions regarding the case, including the decision of whether to settle. This should not preclude the financing entity from providing advice, so long as the right to decide remains with the client and lawyer. The insurance defense practice is an important model that can be used for comparison here. The insurance company retains the right to decide whether to accept or reject a settlement, except perhaps in medical or attorney malpractice

cases. If anything, the financing arrangements discussed here are less intrusive on the attorney-client relationship than is the case in the insurance defense area.

**Evolution of Ethical Rules.** In the end, ethics rules do not pose a significant barrier to the development of third-party financing structures. However, even if they do pose something of a barrier, ethics rules can and do change. As seen in other areas of legal ethics, the rules change to meet the ethical needs of developing commercial markets. The prohibition on lawyers engaging in ancillary businesses has been relaxed. Restrictions on lawyers changing firms have also been relaxed. And given an ever-changing marketplace, we can expect future regulatory revisions that better suit evolving commercial conditions.

### Third-Party Finance: Legal Risk and Its Implications

*Summary of Remarks by Stephen Yeazell, Professor, UCLA School of Law*

The development of alternative financing arrangements will be shaped by actual or perceived legal risks associated with novel financing. One potential concern—although an unlikely one—is whether there might be criminal prosecution based in the wire fraud statute. The wire fraud statute makes it a felony to deprive anyone of the “intangible right to honest services.” Historically, this statute was used to prosecute dishonest public officials, but recently, prosecutors have applied the statute to two new defendant types: private employees who have breached fiduciary duties to their employers and lawyers whose use of an unlawful financing scheme has allegedly deprived their clients of their undivided loyalty. For example, this statute was used to convict William Lerach, a class-action securities lawyer. Federal prosecutors claimed that Lerach’s clients were deprived of his honest services because of an undisclosed financial arrangement.

If a prosecutor thought that third-party funding breached an ethical rule, it could be a federal felony for a lawyer to use this method of financing litigation. While it is unlikely that one of these cases would succeed if brought, the mere possibility of prosecution might influence the development of new funding arrangements.

These speculative prosecutions, or the threat of them, matter because they create uncertainty. There are several consequences of this uncertainty. Lawyers will likely disclose financing arrangements to clients and try to obtain client consent in order to negate any charges of misrepresentation that might arise under the federal wire fraud statute. We might ask what would happen if such a disclosure was made. Clients might withhold consent, put off by the firm’s lack of financial resources to cover the litigation. While the lawyer may give convincing reasons about why third-party financing is a better option, this signal of inadequate intrafirm resources might still raise doubts in clients’ minds.

In addition, it is uncertain whether the attorney-client privilege and work-product privilege apply to third-party financiers. These privileges are most likely applicable in normal contexts, but neither applies to a criminal act. If even one trial judge rules that undisclosed third-party funding might be a crime, those privileges drop away. Finally, the uncertainty could encourage a client whose financed case was unsuccessful to sue, saying that the financing scheme distorted the lawyer’s incentives.

If and when the legal uncertainty that surrounds third-party funding is resolved, there are two likely effects. At the level of the individual case, third-party funding might have a

“branding effect.” Lawyers may happily advertise the availability of litigation financing and begin to do so immediately. The willingness of a third party to assume risk could represent a seal of approval for the underlying cause of action. On the other hand, within the legal profession, certain types of cases that require time and investment currently find their home in a small circle of well-capitalized firms or several firms in a joint venture. Third-party funding has the potential to make some smaller firms contenders for large cases, which may, in turn, cause increased competition with larger firms. It may also serve as a signal to other prospective clients of smaller firms, thus increasing the competitiveness of a new group of firms and expanding the pool of lawyers engaged in particular types of litigation.

## Financing and Firm Management

*Summary of Remarks by Kathleen Flynn Peterson, Partner, Robins, Kaplan, Miller & Ciresi LLP*

The willingness to take on risk using the firm’s capital is an important part of high-risk complex litigation. Third-party funding may change this dynamic by providing resources to clients and attorneys for whom contingency-fee litigation is not feasible. There are significant ethical considerations that must be taken into account, but if third-party funding becomes part of everyday practice, it is likely to have salutary effects.

### The Benefits of Third-Party Financing

**Increased Financial and Talent Resources for Previously Underfunded Clients.** Lawyers’ primary concern regarding third-party funding is the uncertainty about what the ethical considerations may be. Even though these issues can be explained—and were explained during this session—there is still uncertainty about what it might mean for a client if a court concludes that work-product and attorney-client privileges are not protected. But this uncertainty is balanced by the likely good of third-party funding. It helps level the playing field by financing litigants with legitimate claims who cannot otherwise afford to litigate.

**Increased Competition Among Lawyers and Firms.** Third-party financing would also introduce healthy competition among lawyers who handle contingency-fee cases. There is, certainly, a concern that clients might think less of firms that use outside funding: They may look at the competition and wonder why the case cannot be financed by the firm using its own capital. However, third-party funding would not replace all contingency-based litigation. Historically, commercial clients have not entered litigation on a contingency-fee basis, but in the current economic downturn, they do not all have the resources necessary to finance litigation by paying hourly fees and expenses. Third-party funding would allow them to pursue justice by litigating meritorious claims.

**Client Knowledge as Key to Successful Financing Relationships.** These arrangements must be viewed in light of ethical considerations. Third-party funding has the benefits of champerty without the downside. Financiers should not have anything to do with how litigation is handled. There is no reason that third-party funding should interfere with independent professional judgment, and it should not result in more protracted or complex litigation. The conflicts of interest essentially are the same as in contingency-fee cases. The attorneys must ensure that the client fully understands the risks and benefits of either financing scheme.

**Will Third-Party Financing Increase the Number of Lawsuits?**

It is unlikely that there will be a rise in the number of lawsuits as third-party litigation funding becomes more popular. In fact, frivolous and nonmeritorious lawsuits have always been part of the system. The courts are already capable of dealing with these cases through dismissals, summary judgments, and sanctions.

The focus should not be on the number of cases affected by more readily available resources, but on the merits of cases. Continued research and discussion among professionals is needed. The degree of discipline that must be brought to risk analysis cannot be stressed strongly enough. It is very difficult to look at a case thoroughly and judge whether it is worthy of going forward. There are many failed firms that entered the contingency-fee arena and did not make these judgments accurately. We should pay attention as third-party financers bring their expertise in risk analysis to complex high-stakes litigation.



## Roundtable Discussion Summary

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The conference concluded with a question-and-answer period, conducted between the audience and the conference presenters. The session highlighted the many perspectives from which the topic of novel funding was examined. Some of the key points of this roundtable discussion session are recounted here.

### What Is the Role of Regulation in an Emerging Industry?

The first questioner invited Selwyn Seidel to elaborate on his ideas of appropriate regulation for this emerging industry. Seidel stated that, while we may already know some of the needed regulations, others are yet unknown. The role of self-regulation is currently under investigation by scholars, and some studies in the United Kingdom have already considered different regulatory frameworks for the industry.

In the meantime, one area of regulation that needs immediate attention concerns claimants. Such regulation should require claimants to provide financiers full disclosure. The market has suffered from claimants trying “to pull the wool over people’s eyes” by failing to disclose to financiers all relevant information. This has made it more difficult for proper risk allocation and has slowed down the funding process. For claims that are approved and to be prosecuted, a certain degree of cooperation and disclosure from claimants and lawyers is necessary as proceedings move forward. Without this, financiers are reluctant to finance claims.

Regulation is not the only solution to this problem, however. Contract provisions could require claimants to provide certain disclosures prior to any funding agreement. However, contract provisions are not effective enough because it is too easy to “get off the hook” and avoid contract provisions.

Different forms of regulation might apply to third-party financing. Regulation of financial providers might take the form of licensing. Financiers may need to pass certain requirements to demonstrate that they have both capital and credibility. There may also be a need to ensure that financiers will fulfill their obligations. If they fail to fulfill certain obligations imposed by the industry, industry-imposed penalties and negative publicity are needed. Another option, self-regulation, can provide necessary guidance to the industry. Although the United States had negative experiences with self-regulation in the financial industry, this does not mean that self-regulation does not work as a matter of course. In addition to self-regulation and licensing efforts, financiers need rules laid down by courts that regulate the industry’s activity in a coherent way. In response to a question about the U.S. federal structure and the proper regulator (federal versus state oversight), federal and state regulation may be a likely result.

In conclusion, in-depth, systematic study of how the U.S. industry and its segments operate—including data collection and analysis—is necessary. Policy options or recommendations are also required, including suggestions for how to regulate the various segments (if at all).

Tim Scrantom offered his thoughts on the regulatory question. The third-party litigation finance industry developed out of legislation passed in the United Kingdom two years ago. Because of that, the UK industry is responding to a new market. In contrast, the question currently presented in the United States concerns how to take an existing marketplace for contingency-fee arrangements and find ways to regulate what *has been*, rather than what will be.

### **What Are the Funding Opportunities for the Defense?**

The second question addressed to the panel asked how and where funding would apply on the defense side, when it was clear what role it could play when used by a plaintiff who needs funds to prosecute. James Tyrrell responded by offering two hypothetical situations to the audience. Imagine a client who faces a suit and wants to file a motion for summary judgment against the plaintiffs. The client may approach the defense counsel and say, “The cost of making a summary judgment motion is \$100,000. I want to bring the motion but do not want to pay that price for it. If you truly believe in the motion’s likely success, I will pay you \$50,000 to bring the motion, and if you win, I’ll give you \$200,000—a portion of the value to the client of winning the motion.” If the attorney will not take the \$50,000 risk to bring the motion, he or she can ask an outside financier to share the risk. In other words, the financier can invest the other \$50,000 to bring the motion and recover a potential windfall if the motion succeeds.

A more sophisticated issue where defense side funding might play a role involves insurance companies and corporations that have to reserve pools of money for potential claims against their assets. If a company is sued, it can estimate the potential losses it would suffer under a losing defense (for example, a company might estimate its likely losses at \$600 million). If the company chooses, it could reach an agreement with a funder who would fund the defense (or some part of it) in exchange for some portion of the amount by which the damages fall below \$600 million after the case is resolved. If, in the best-case scenario, the case results in a complete defense verdict, the funder might receive, for example, \$200 million—i.e., one-third of the defendant’s gain of \$600 million—because it eliminated, at its own expense, a risk the company valued at \$600 million.

Jonathan Molot also suggested that litigation defendants want not just protection against legal fees like plaintiffs do, but also protection against the downside risk of a large adverse judgment. This is what has made third-party litigation funding more difficult on the defense side than on the plaintiff side. For plaintiffs, the situation can be likened to buying options, betting pennies to make dollars. On the defense side, however, it is more like insurance, risking dollars to make pennies. That financial reality does not mean that defense financing cannot be done. A firm would need a big balance sheet to do it, so insurance companies may be best suited because they are highly leveraged. If an insurance company had to pay all its claims at once, it would go bankrupt. However, it proceeds on the assumption that this will not happen as it goes through actuarial analysis.

The reason that it has been difficult to get insurance companies to buy into third-party financing is an example of the pricing problem mentioned in the discussion of litigation markets and litigation accuracy in session 2. Insurers do not view litigation risk as being subject to actuarial pricing. If an insurer is evaluating the likelihood of a litigation-triggering event—a mass tort, something going wrong—then it can play the law of large numbers and estimate



what it thinks the policyholder's premium should be. But the case of after-the-event insurance is a different concept. The distinction is between the risk of a litigation event *happening* and the risk of having a litigation *outcome*. Insurers are not used to insuring litigation outcomes and may be reluctant to get into the practice. This does not mean that it cannot be done, however.

Molot said that the panelists at the conference and the hedge funds behind them are willing to bet on litigation and are willing to take the risk. However, the hedge funds do not have the balance sheet to support broad and potentially very expensive defense funding.

Timothy Scrantom raised a point about nomenclature, reminding the audience that, during the conference, there were references to insurance, funding, litigation funding, claim transfer, after-the-event insurance, and before-the-event insurance. The multiplicity of terms can be confusing, and a new set of words to describe some of these phenomena may be required. The core issue, however, is the distribution of risk associated with litigation.

### **How Can the United States Overcome the Stigma Associated with Third-Party Litigation?**

Another query asked the panel about the stigma involved with third-party funding. Although the practice is growing in foreign jurisdictions and gaining ground in the United States, the stigma against third-party financing might be formidable. The stigma is managed in foreign jurisdictions through institutional acceptance, leadership by members of the judiciary, and law firms that championed third-party funding in the absence of contingency-fee arrangements.

Jonathan Molot responded by pointing out that there are primary differences in the U.S. and UK approaches. In the United Kingdom, lawyers are not allowed to finance cases (no contingency-fee arrangements), but third-party financiers are permitted to advance capital. In the United States, generally, third-party capital providers are not allowed, but lawyers may finance the cases they represent. Part of the challenge the United States faces—a problem that arises primarily because of a tradition of lawyer involvement—is the stigma against profiting from someone else's harm. This stigma has been institutionalized in the United States, although it did not prevent the acceptance of contingency-fee arrangements.

This stigma against third-party financing works in collaboration with the monopoly enjoyed by contingency-fee attorneys—an odd arrangement, given the stigma against profiting off of harm. Counter to the stigma, third-party financing would break this monopoly on financial arrangements, providing competition among those who would seek to invest in a claim.

Other participants noted that, once the “AmLaw 100” (American Lawyer 100) firms and the well-regarded plaintiffs' firms begin to make greater use of third-party financiers, it will be a *fait accompli*. The stigma will fall away in light of third-party financiers' usefulness.

### **Will the Quality of Claims Be Affected by Increased Access to Funding?**

One audience member noted the trend of bigger and more expensive lawsuits and asked the panelists if they thought third-party litigation finance could be designed to increase not only the quantity of funding for litigation but also the quality of claims that are being brought, and whether this would mean an improvement in the just resolution of conflicts.

Jonathan Molot responded by echoing the idea that an imbalance in resources gets in the way of just resolution. The ideal solution is not adding more money to balance out the resource allocation, but to design a litigation system that is more predictable and less costly overall. This issue is the very one that lawyers, judges, and law professors constantly address, but they have

yet to come up with a working solution. Working toward such a litigation system is the noblest goal, to be sure, but such efforts have yielded few immediate dividends. As an alternative or a short-term approach, third-party litigation finance is a less perfect but perhaps more realistic solution.

## Concluding Remarks

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The daylong conference achieved what it was designed to do: provide an open forum for exploring and considering the deeper implications of litigation financing alternatives in the United States and Europe. These conference proceedings present some options and potential implications. The issues that the conference participants discussed are timely and point toward potentially significant effects on the operation and outcomes of the civil justice system. As other countries explore and implement creative financing options for litigation, the United States should consider the social advantages and disadvantages of nontraditional forms of litigation finance.



## **Conference Materials**

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This appendix includes the agenda, presenter bios, and list of participants, which were provided to conference attendees. The materials are unedited, and the content was current at the time of the conference.



## Third Party Litigation Funding and Claim Transfer: Trends and Implications for the Civil Justice System

Tuesday, June 2, 2009

8:00 a.m.—2:00 p.m.

[The RAND Corporation](#)

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Welcome to the  
Third Party Litigation Funding and Claim Transfer  
Trends and Implications for the Civil Justice System  
 Policy Symposium

June 2, 2009

Dear Participants,

On behalf of the UCLA-RAND Center for Law and Public Policy, we are pleased to welcome you to our 2009 Symposium, Third Party Litigation Funding and Claim Transfer: Trends and Implications for the Civil Justice System. Your time and interest are much appreciated and essential to a robust interchange of ideas and perspectives among experts and stakeholders.

The conference agenda is designed to identify and analyze an emerging international trend in civil justice: litigation claim transfer (also referred to as third party litigation funding). While the practice is gaining prominence in Europe, Canada and Australia, the confluence of the recent credit shortage, the scale of the overall market for legal services, and the search for investment opportunities unrelated to general economic risk has created the environment for debate about its role, if any, in the American civil justice system.

The agenda is designed to encourage interaction among participants while providing a rigorous academic framework. Our goal is to facilitate a timely dialogue to discuss the risks and opportunities associated with the confluence of law and finance as well as to elevate how it is debated by lawyers, regulators, policymakers, academics and rule makers.

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**Third Party Litigation Funding and Claim Transfer:  
*Trends and Implications for the Civil Justice System***

RAND Corporation  
1776 Main Street, Santa Monica, CA  
June 2, 2009

Agenda

- 8:00 am**      **Continental Breakfast and Networking**
- 8:15 am**      **Introduction and Welcoming Remarks**  
*Dean Michael Schill, UCLA School of Law*
- 8:20 am**      **Framing the Central Issues: On What Bases Should Financing Be Evaluated?**  
*Lynn M. LoPucki, UCLA School of Law*
- 8:35 am**      **Litigation Financing Overview**  
*Selvyn Seidel, Burford Advisors*
- 8:50 am**      **The Traditional Landscape: Funding of Claims in the US**  
Moderated by: *Fred Kipperman, RAND*  
Featured Panel: *Herbert M. Kritzer, University of Minnesota; Neil Rickman, RAND; and James E. Tyrrell, Jr., Patton Boggs LLP*
- 9:40 am**      **Market Financing: U.S. Developments in Claim Transfer and Third Party Funding**  
Moderated by: *Joseph W. Doherty, UCLA School of Law*  
Featured Panel: *Timothy D. Scramton, Juridica Capital Management (US), Inc. and Jonathan T. Molot, Georgetown University Law Center*
- 10:30 am**      **Existing Rules, Regulations and Restrictions on Claim Transfer and Third Party Funding**  
Moderated by: *Neil Rickman, RAND*  
Featured Panel: *Stephen C. Yeazell, UCLA School of Law; Nathan M. Crystal, Charleston Law School; and Kathleen Flynn Peterson, Robins, Kaplan, Miller & Ciresi L.L.P.*
- 11:30 am**      **Coffee Break**
- 11:45 am**      **Roundtable: Emerging Commercial, Legal and Ethical Considerations**  
Moderated by: *Robert T. Reville, RAND*
- 12:30 pm**      **Concluding Remarks and Summary**  
*James N. Dertouzos, RAND*
- 12:35 pm**      **Pre-Lunch Break**
- 12:45 pm**      **Lunch in the RAND Courtyard**  
*Sponsored by IM Litigation Funding*
- 1:00 pm**      **Keynote Address by Lord Daniel Brennan QC**
- 2:00 pm**      **Adjourn**



## UCLA-RAND Center for Law and Public Policy

### Third Party Litigation Funding and Claim Transfer: Trends and Implications for the Civil Justice System

#### *Presenter Biographies*

#### **Keynote Speaker**

##### ***Lord Daniel Brennan QC***

Lord Daniel Brennan QC specializes in commercial law, international business issues, public and private international law, and international arbitration. During 1999, he was Chairman of the Bar of England and Wales, the organization that represents 10,000 practicing barristers—specialist advocates and advisers in litigation and in 2000, he was voted Barrister of the Year. In May 2000, the Queen, on the recommendation of the United Kingdom Government, appointed him a life peer and member of the House of Lords.

He is a Deputy High Court Judge and Crown Court Recorder, a former member of the Criminal Injuries Compensation Board, and ex-Chairman of the Personal Injury Bar Association. He also is Chairman of Juridica Capital Management Limited. He has a high profile environmental, product liability and medical negligence practice involving multi-party actions such as the insurance claims from the Paddington rail crash, the oral contraceptive litigation and, in the past, the local residents' claims arising from the Canary Wharf development scheme, the HIV/haemophiliac claims against the UK government and the Herald of Free Enterprise disaster. Most recently he has appeared in the 'designer baby' appeal in the House of Lords. He also has an extensive international litigation and advisory practice involving bi-lateral investment treaty and commercial and energy work in South America and Asia.

Lord Brennan is currently the Bar representative on the Council of the International Bar Association. He is also a member of the London Court of International Arbitration and a member of the Arbitration Foundation of South Africa, as well as a member of its Appeals Panel. South Africa. He is also on the panel of consultants to the World Bank for Latin America and South and East Asia.

#### **Speakers and Panelists**

##### ***Nathan Crystal, Charleston Law School***

Nathan Crystal is a Distinguished Visiting Professor of Law at the Charleston Law School. He taught for 32 years at the University of South Carolina School of Law until he retired in 2008. On his retirement from South Carolina he was named the Distinguished Class of 1969 Professor of Professional Responsibility and Contract Law Emeritus. He holds degrees from the University of Pennsylvania (Wharton School), Emory Law School (where he was editor-in-chief of the law review), and Harvard Law School. Professor Crystal concentrates in the areas of professional responsibility and contract law. He is the author or coauthor of four books, three on legal ethics and one on contract law, including: *Professional Responsibility – Problems of Practice and the Profession* (Aspen Law & Business 4th ed. 2008); *An Introduction to Professional Responsibility* (Aspen Law & Business 1998); *Annotated South Carolina Rules of Professional Conduct*

(S.C. Bar 2009 ed., with Robert M. Wilcox, forthcoming in June); and *Problems in Contract Law: Cases and Materials* (with Charles Knapp and Harry G. Prince, 6<sup>th</sup> ed. 2007).

In addition to his books, Professor Crystal has published numerous articles in scholarly journals and authors a bimonthly column, "Ethics Watch," for the South Carolina Lawyer. Professor Crystal lectures frequently on matters of professional ethics to national, regional, and local organizations, including the American Bar Association and the United States Justice Department. He has been a member of the South Carolina Bar Ethics Advisory Committee for more than 20 years and served as chair of the Committee from 2002-2003. Professor Crystal was associate dean of the USC Law School from 1987-1992 and director of its Center on the Legal Profession from 1991-1999. He has held visiting appointments and lectureships at Arkansas (Little Rock), Florida State, Hastings, Indiana (Indianapolis), Luiss (Rome), Scuola Superiore Santa'Anna (Pisa), Suffolk, Sydney (Parsons Visiting Scholar).

### ***James N. Dertouzos, RAND Corporation***

James N. Dertouzos is Acting Director of the Institute for Civil Justice (ICJ). During his 27-year tenure at RAND, Dr. Dertouzos has led over 100 research projects and has served in a variety of management positions, including Associate Head of the Economics and Statistics Department, Associate Corporate Research Manager, and Resident Scholar in Economics. In addition to his research activities, he served as senior advisor to the Volcker Commission on Public Service, is a faculty member of the Pardee RAND Graduate School for Policy Studies and has taught courses at Stanford, UCLA, and the University of Southern California.

Dr. Dertouzos' research and publications cover a wide range of public policy issues including public sector management, the industrial organization of mass media, and military manpower. His ICJ research has included studies on wrongful termination in the late 1980s as well as more recent work on the legal and economic implications of electronic discovery. With support from the Sloan Foundation, he previously directed an ICJ project on the legal and economic consequences of the increasing labor market liability of employers. Dr. Dertouzos received his PhD in economics from Stanford University in 1980.

### ***Herbert Kritzer, University of Minnesota***

Herbert (aka "Bert") Kritzer will become Professor of Law and Affiliated Professor of Political Science at the University of Minnesota on July 1, 2009. Since July 2007 he has been Professor of Law at William Mitchell College of Law. Prior to moving to the Twin Cities, Professor Kritzer taught at the University of Wisconsin-Madison from 1977 until 2007, becoming *Emeritus* Professor of Political Science and Law in May 2007. He holds a Ph.D. in Political Science from the University of North Carolina at Chapel Hill (1974) and a B.A. in Sociology from Haverford College (1969).

Professor Kritzer is the author or coauthor of five books, coeditor of a sixth book, editor of a four volume encyclopedia (*Legal Systems of the World*), and the author of over 100 journal articles or book chapters. He is currently coediting the *Oxford Handbook of Empirical Legal Studies*.

Professor Kritzer's research focuses on the empirical study of the legal profession and a variety of legal phenomena. Current projects include several studies related to scientific and expert testimony, judicial elections, television news coverage of litigation and the legal profession, the craft of legal practice, access to justice, and the defense of tort claims. His research involves a combination of quantitative and qualitative

methodologies including the analysis of data derived from institutional records, systematic surveys, semi-structured interviews, and ethnographic-style observation.

### ***Lynn M. LoPucki, UCLA School of Law***

Lynn M. LoPucki is the Security Pacific Bank Professor of Law at the UCLA Law School, and, each fall semester, the Bruce W. Nichols Visiting Professor of Law at the Harvard Law School. He teaches Secured Transactions and Empirical Analysis of Law at both schools.

Professor LoPucki has engaged in empirical research on large public company bankruptcies for the past twenty-five years and has been quoted in several hundred news articles on the topic in just the past five. His Bankruptcy Research Database <http://lopucki.law.ucla.edu> provides data for much, if not most, empirical work on the topic. Professor LoPucki's book, *Courting Failure: How Competition for Big Cases Is Corrupting the Bankruptcy Courts* (University of Michigan Press 2005) shocked the bankruptcy world with empirical evidence regarding the effects of forum shopping and court competition. The debate over those allegations has dominated recent scholarship in the field. Professor LoPucki and his frequent coauthor, Joseph W. Doherty, are currently working on another book, *Controlling Professional Fees in Corporate Bankruptcies*, under contract with Oxford University Press.

Professor LoPucki uses an empirically-based systems approach for policy analysis. He has recently proposed public identities as the solution to identify theft, court system transparency as the solution to judicial bias, and an effective filing system as the solution to the deceptive nature of secured credit.

Professor LoPucki is co-author of two widely used casebooks: *Secured Credit: A Systems Approach* (5th edition, with Elizabeth Warren, 2006) and *Commercial Transactions: A Systems Approach* (with Warren, Keating, and Mann, 3rd edition, 2006) a leading practice manual: *Strategies for Creditors in Bankruptcy Proceedings* (with Christopher R. Mirick, 5th edition, 2007) and a popular series of bankruptcy procedure flow charts: *Bankruptcy Visuals*. LoPucki's *Death of Liability* thesis – propounded in a *Yale Law Journal* article in 1996 – is featured in casebooks in several fields. Professor LoPucki received his B.A. and juris doctor from University of Michigan and an LL.M. from Harvard.

### ***Jonathan Molot, Georgetown University Law Center***

Professor Molot writes and teaches at Georgetown University Law Center in the fields of civil procedure, complex litigation, administrative law, statutory interpretation, federal courts, corporate finance, and insurance law. His articles have appeared in the *Yale Law Journal*, the *Stanford Law Review*, the *Columbia Law Review*, the *Virginia Law Review*, and *The University of Chicago Law Review*. Professor Molot has worked with law firms, investment funds, investment banks, and insurance companies and brokers on various structures to manage and transfer litigation risk. Before entering law teaching, Professor Molot clerked for Justice Breyer on the U.S. Supreme Court and practiced law at Cleary, Gottlieb, Steen & Hamilton in New York, and at Kellogg, Huber, Hansen, Todd, Evans & Figel in Washington, D.C. He graduated *magna cum laude* from Yale College and *magna cum laude* from Harvard Law School, where he was Articles Co-Chair of the *Harvard Law Review* and won the Sears Prize (awarded to two students with highest GPAs in a class of more than 500). Professor Molot was a Visiting Professor at Harvard Law School in the fall of 2007 and served as a lawyer on the Obama Transition Team and Obama Treasury Department during the Fall and Winter of 2008-2009.

***Kathleen Flynn Peterson, Robins, Kaplan, Miller & Ciresi LLP***

Kathleen Flynn Peterson is a partner with the national law firm of Robins, Kaplan, Miller & Ciresi L.L.P. and a Civil Trial Specialist certified by the Civil Litigation Section of the Minnesota State Bar Association. Kathleen limits her practice to medical malpractice representing individuals and families who have experienced injury or death as a result of medical negligence. Kathleen currently serves as President of the American Association for Justice and is a member of the RAND Institute for Civil Justice Board of Overseers. She is the 1999 recipient of ATLA's Lifetime Achievement Award. She is a member of the International Academy of Trial Lawyers, the International Society of Barristers, the American College of Trial Lawyers and the American Board of Trial Advocates, serving as President of Minnesota's ABOTA chapter in 2005. She is Past President of the Minnesota Trial Lawyers Association.

Ms. Flynn Peterson's verdicts and settlements have consistently been reported among the highest in Minnesota. She has been repeatedly named in Best Lawyers in America and Law & Leading Attorneys and was named one of the 25 Women Industry Leaders by the Minneapolis/St. Paul Business Journal, 2006. In 2007 she was named by the National Law Journal as one of the 50 Most Influential Women Lawyers, and was named by Minnesota Lawyer as an Attorney of the Year. She received her B.A. in nursing from the College of Saint Catherine in 1976, and her law degree from William Mitchell College of Law in 1981.

***Robert T. Reville, RAND Institute for Civil Justice***

Robert Reville is the Director of the RAND Institute for Civil Justice (ICJ) and the Director of the Center for Corporate Ethics and Governance (CCEG). He was appointed Director of the ICJ in October 2002, after serving as research director for three years.

As a labor economist, Dr. Reville focuses on compensation policy, and has a national reputation in workplace injury compensation policy and the impact of disability on employment. He was recently appointed to the Board of Scientific Counselors of the National Institute for Occupational Safety and Health (NIOSH), Centers for Disease Control and Prevention. He also serves on the Workers' Compensation Steering Committee of the National Academy of Social Insurance. As Director of the Institute for Civil Justice, Dr. Reville leads a highly-respected research organization within RAND that provides empirical research to inform policy decision making on class actions and mass torts, jury verdicts, administration of justice, workers' compensation and other civil justice issues. As a founding Co-Director of the Center for Terrorism Risk Management Policy, Dr. Reville has built a center within RAND to address policy issues related to terrorism victims' compensation, liability, risk management, risk modeling and insurance.

Currently, Dr. Reville is leading an innovative project to create models and information products related to mass litigation. The project is a joint venture between RAND Institute for Civil Justice (ICJ) and Risk Management Solutions (RMS). The ICJ will use the resulting models and databases for public policy applications. Dr. Reville received his Ph.D. in economics from Brown University.

***Neil Rickman, RAND Institute for Civil Justice Europe***

Neil Rickman is Director of RAND Europe's newly created Institute for Civil Justice Europe and Professor of Economics at the University of Surrey.

Neil graduated from the University of Durham (BA (Hons) Econ) in 1988, before moving to McGill University (Montreal) to read for a PhD in Economics, which was completed in 1995. From 1991 to 1995 he was a Research Officer in Economics at the Centre for Socio-Legal Studies, Oxford, and a lecturer in Economics at Pembroke College, Oxford. He moved to Surrey in 1995, and became Professor of Economics, and Head of the Department of Economics, in 2004. He is a CEPR (Public Policy) Research Affiliate and became Chair of the Royal Economic Society's Conference of Heads of University Departments of Economics (CHUDE) in January 2007. He is a member of the Editorial Board of the *International Review of Law and Economics* and also of the Government Economic Service's Professional Training Board.

Neil's research interests are in the regulation of service industries, especially in legal services and health care. In these areas, he has published research on medical negligence, legal aid reform, contingent fees for legal services, legal expenses insurance, litigation, medical malpractice and NHS contracts. He has advised the Ministry of Justice, the Legal Services Commission, the Law Society, the Civil Justice Council and the Department of Health on matters relating to legal policy and medical malpractice. He has also advised Ofcom on radio spectrum regulation. His work for the Civil Justice Council in 2003 (with Paul Fenn, University of Nottingham) helped establish the current regime of fixed fees for road traffic accident litigation in England and Wales. Neil was a member of the Civil Justice Council's sub-committee on Court Fees (2000-2002) and the Advisory Panel for Sir David Clementi's Review of the Regulatory Framework for Legal Services in England and Wales (2004); he was also invited to give advice to Lord Woolf's Review of Civil Procedure in England and Wales (1995). He is currently an advisor to the National Audit Office's value for money study of criminal legal aid in England and Wales.

Neil has published in the *Economic Journal*, the *Journal of Public Economics*, *Economica*, *Oxford Economic Papers*, the *Journal of Health Economics*, the *Journal of Risk and Insurance*, the *Scottish Journal of Political Economy*, *Fiscal Studies*, the *British Medical Journal*, the *International Review of Law and Economics*, the *Oxford Review of Economic Policy*, the *Geneva Papers on Risk and Insurance* and the *European Journal of Law and Economics*. He has also authored/co-authored seven reports for the Ministry of Justice, others for the Legal Services Commission, Civil Justice Council and Department of Health, and numerous book chapters.

***Michael Schill, UCLA School of Law***

Michael Schill is Dean and Professor of Law at UCLA School of Law. Dean Schill is a national expert on real estate and housing policy, deregulation, finance and discrimination. He has written or edited three books and over 40 articles on various aspects of housing, real estate and property law. He is an active member of a variety of public advisory councils, editorial boards and community organizations. Before joining the faculty of UCLA School of Law, Dean Schill was the Wilf Family Professor in Property Law at New York University School of Law and professor of urban planning at NYU's Robert F. Wagner Graduate School of Public Service. From 1994 to 2004, Dean Schill served as the director of the Furman Center for Real Estate and Urban Policy. Prior to that, Schill was a tenured professor of law and real estate at the University of Pennsylvania. He has also been a visiting professor at Harvard Law School.

***Timothy D. Scrantom, Juridica Capital Management Limited***

Timothy D. Scrantom is the President of Juridica Capital Management (US), Inc. He is an American lawyer and an English barrister-at-law (Gray's Inn) (currently non-practicing). In private practice, a significant portion of his practice centered on disputes, audits and investigations in international finance. He also acted as a strategic consultant on legal issues in complex multi-jurisdiction litigation and business migrations.

Mr. Scrantom received a juris doctor (*cum laude*) from the University of Georgia (1983) and an LL.M. in International Business Law from the London School of Economics (1984). In the United States, he is admitted to practice in the District of Columbia, Georgia and South Carolina. Mr. Scrantom is a barrister before the courts of the Eastern Caribbean States.

***Selvyn Seidel, Burford Advisors***

Selvyn Seidel is an attorney with 40 years experience representing business entities in diverse projects in the United States and abroad. Until December 31, 2006, he was a senior partner at Latham & Watkins, a leading international law firm. At Latham, Mr. Seidel was at different times the Chairman of its International Practice, the founder and Chairman of its International Litigation and Arbitration Practice Group, and the Chairman of its New York litigation department.

He was for ten years an Adjunct Professor at New York University School of Law, where he taught courses in International and National jurisdiction and practice. He is currently an Alumnus Lecturer at Linacre College, Oxford University.

Mr. Seidel is the founder, Chairman, and CEO of Burford Advisors LLC, and its subsidiary Burford Litigation Funding. The entities consist of diverse, experienced professionals, and distinguished business and finance individuals, advising on an integrated and comprehensive basis. In the litigation finance industry, Burford Litigation Funding and members of Burford Advisors LLC are independent expert consultants to Claimants, Funders, insurance entities, and law firms. As such, they assist on a number of levels: matching Claimants with Funders, insurance entities, and law firms, as needed; independently and objectively evaluating Claims, and when possible improving the recovery value of the Claim; facilitating the approval process of Claims; coordinating with various parties and improving where possible the prosecution of and resolution of Claims; assisting in establishing Funds for special areas of litigation financing.

Mr. Seidel graduated from the University of Chicago (1964, B.A., economics), the University of California (Berkeley) law school (1967, J.D., California Law Review), and the University of Oxford (1968, Dip. Law, Linacre College).

***James E. Tyrrell Jr., Patton Boggs LLP***

James E. Tyrrell, Jr. is the Managing Partner of the Greater New York/New Jersey offices of Patton Boggs, National Chair of the firm's Toxic Tort and Product Liability practice groups, and a member of its Executive Committee. Mr. Tyrrell's experience includes toxic tort, product liability, intellectual property, antitrust, and general commercial litigation.

In the area of toxic torts, Mr. Tyrrell served as chief trial counsel for a prominent agricultural company in Agent Orange litigation, national coordinating counsel for a leading research-based pharmaceutical company in the DES litigation, national counsel for the largest American-owned wine and spirits business in alcohol-related litigation, chief science counsel in litigation involving a world-leading steel manufacturer and distributor, and counsel for one of the ten largest Fortune 100 companies in silicon gel breast implant litigation. Mr. Tyrrell also serves as product liability counsel for a PCBs and chemicals corporation, a large consumer product and toy company, and numerous other manufacturers.

In the developing areas of intellectual property litigation and e-commerce, Mr. Tyrrell serves as national coordinating counsel for a technologies company, representing it on a wide range of intellectual property and trade secret cases. Mr. Tyrrell also represents numerous communications companies and other leading corporations across many industries.

After serving as an associate at a large law firm, Mr. Tyrrell became the youngest equity partner with another notable firm in Manhattan. In other law firm experience before coming to Patton Boggs, Mr. Tyrrell was a senior partner and headed one firm's largest litigation team, and he was later the Managing Partner of the New Jersey office of a highly-ranked Am Law 100 firm. Mr. Tyrrell also served as a Lieutenant in the Navy Judge Advocate General's Corps.

A member of numerous associations, Mr. Tyrrell has served on the Federal Legislation Committee and currently serves as Chairman of the Board of Directors of the Reflex Sympathetic Dystrophy Syndrome Association of America.

### ***Stephen C. Yeazell, UCLA School of Law***

Stephen Yeazell is the *David G. Price and Dallas P. Price Professor of Law* at the UCLA School of Law. He has written about the history and theory of procedure and about the contemporary transformation of civil litigation, including its financing mechanisms. He teaches courses that correspond to the following interests: Civil Procedure, Contemporary Civil Litigation, and International Civil Litigation. He has received the University's Distinguished Teaching Award and was the first recipient of the School of Law's Rutter Award for Excellence in Teaching. He served as chair of the UCLA Academic Senate for 2000-2001 and as Associate Dean of the School of Law from 1995 to 1998.

Professor Yeazell's books include *From Medieval Group Litigation to the Modern Class Action* (1987) and *Civil Procedure* (7th ed., 2008). Articles pertinent to today's symposium include: *Refinancing Civil Litigation*, 51 De Paul Law Review 183 (2001), *Getting What We Asked For, Getting What We Paid For, and Not Liking What We Got*, 1 J. of Empirical Legal Studies 943 (2004), and *Brown, the Civil Rights Movement, and the Silent Litigation Revolution*, 57 Vanderbilt Law Review 1975 (2004). Professor Yeazell received his B.A. from Swarthmore, his M.A. in English and Comparative Literature from Columbia, and his J.D. from Harvard.

**Third Party Litigation Funding and Claim Transfer:  
*Trends and Implications for the Civil Justice System***

RAND Corporation  
1776 Main Street, Santa Monica, CA  
June 2, 2009

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## **Presenter Materials**

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This appendix includes the text of the keynote address by Lord Daniel Brennan, presentation slides, and an overview of the purpose of the conference, along with references that provide additional background on the conference topic. All materials are unedited, and the content was current at the time of the conference.



## Third Party Litigation Funding and Claim Transfer: Trends and Implications for the Civil Justice System

Tuesday, June 2, 2009

8:00 a.m.—2:00 p.m.

[The RAND Corporation](#)

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# THIRD PARTY LITIGATION FUNDING AND CLAIM TRANSFER

## A COMMON PERSPECTIVE FROM COMMON LAW

Keynote Speech by  
*Lord Daniel Brennan QC*  
June 2, 2009

## THIRD PARTY LITIGATION FUNDING AND CLAIM TRANSFER

### A COMMON PERSPECTIVE FROM COMMON LAW

#### INTRODUCTION

I thank the Rand Corporation and UCLA Law School for their invitation to speak to you today. It does honour to my profession – the Bar of England and Wales. It invokes humility from me as your 13<sup>th</sup> speaker on this important topic. But I am fortified in this task by remembering the quip we have about each other in the House of Lords – “everything has been said on this subject ... but not yet by me!”

I speak as a UK legislator – with experience of recent relevant and significant statutory reform affecting the funding of the civil law system. I also draw on my common law practice as an English barrister – English because the Scottish have a different jurisprudence and practice, and in Northern Ireland they have an independent legal system. Churchill’s remark of our two nations – “united by a common heritage, but divided by a common language” – is usually noted because of its second part. However a substantial component in our common heritage is the common law. That should provide a foundation for seeking a shared view on today’s topic.

Nevertheless in such a sensitive area I will heed the cautionary words of Alexis de Tocqueville on our respective peoples. On the Americans:

“I cannot help fearing that men may reach a point where they look on every new thing as a danger, every innovation as a toilsome trouble, every social advance as a first step toward revolution, and that they may absolutely refuse to move at all.”

On my countrymen:

“The British see things very clearly, but they only see one thing at a time”!

#### THE ISSUE BEFORE US

It is of contemporary importance. It needs to be fully worked out. Should there be access for the capital markets into the civil legal system? Is this a key to perceived current problems of financing litigation?

Lewis Carroll’s Alice in Wonderland may not have been thinking about access to justice when she could not discover how to gain access to the beautiful garden because:

“There were doors all around the hall but they were all locked ...”

and then Alice finds a key but:

“... alas either the locks were too large or the key was too small ...”



although eventually Alice is successful when she:

“... tried the little golden key in the lock and to her great delight it fitted”

Today we are dealing with a key if not the golden key. Many legal systems are facing similar problems about the cost of modern litigation – especially in product liability, environmental claims and commercial disputes. There may be different factors and different emphases as to solutions. But they all involve funding and the cost to the community if the funding is not efficient or indeed available within the legal system.

I use the word “community” deliberately. The legal profession is part of the general economy, and an important part. In the UK law firms provide over 1 million jobs – about 4% of all employment and nearly 3% of GDP. London lawyers earn about \$3 billion from foreign work alone. The US position is probably similar. In the modern business world law firms are the vehicles for major financial transactions – mergers and acquisitions, infrastructure, trade and financial services.

It is implausible therefore to conceive the civil legal system as being insulated and economically separable as to the funding of litigation and claim transfer. Yet the common law for long resisted any third party financial involvement as inimical to the fair administration of justice – what now in the twenty first century?

Let us consider:

- first principles
- recent English and international experience
- US developments
- the utility of third party funding and claim transfer
- safeguards
- the example of Juridica
- the future

## FIRST PRINCIPLES

I anticipate you will all know them – but I will state them anyway. To do so reflects the well known English appeal in a contract case. The appellants’ barrister began to open the basic law of contract to the Court of Appeal – offer, acceptance and consideration, at which the senior Appeal Judge commented with irritation “I think you can assume that any judge understands the basic law” to which the barrister quickly replied “My Lords, that is the very mistake I made in the Court below.”!

1. What the law seeks to provide – an accessible court system.
- A colleague of mine has referred to the antiquity of this objective:

“The fundamental availability of an accessible Court system has a long history. The book of Exodus at chap.18,v.13 describes early access to a judicial process for the resolution of disputes:

“Moses’ father-in-law ... said what is this thing that you are doing to the people? ...and Moses said ... when they have a matter they come unto me and I judge between one and another and I do make them know the statutes of God and his laws ... And Moses’ father-in-law said ... thou shalt provide out of all the people, able men who fear God, men of truth and let them judge the people at all seasons, and it shall be that every major dispute they will bring to you, but every minor dispute they themselves will judge. And they judged the people at all seasons; the difficult dispute they would bring to Moses but every minor dispute they themselves would judge”.

It may be far fetched to suggest that Moses was the architect of the first small claims court but it is not stretching it to acknowledge that the first literary confirmation of access to the due process of jury trial is found in the Greek tragedy “Eumenides”, part of the Oresteia trilogy by Aeschylus. Orestes is on trial for murdering his mother. In charge of the proceedings is the Goddess Athena who thus proclaims her duty to ensure a fair trial:

“The affair is too grave if any mortal thinks to pass judgment thereon, nay it is not lawful even for me to decide on cases of murder which involves swift wrath. I will appoint judges of homicide bound by oath and establish a tribunal to endure for all time. Do ye call your witnesses and adduce your proofs, sworn, evidence to support your cause ... The word is with you, the trial may proceed and ‘tis sound law and justice both that he who doth proffer the charge shall first begin.” ”

[M. Napier – Gresham College Lecture, 20 June, 2007]

Henry II made the real foundations of the English legal system. It was later accepted that access to courts “depends on your means”. This was recognised in Henry VII’s statute of 1494 “in forma pauperis”. Exemption from court fees and access to pro bono lawyers was to be available to:

“every poor person ... and the Lord Chancellor shall assign ... learned counsel and attorneys for the same without reward”

Over the following centuries we have evolved the court system and access to it to meet the needs of the time.

So we can fairly conclude that nowadays society can expect a court system that works and access to it is economically reasonable.

## 2. Third Party financing of litigation (from an English perspective).

In the fourteenth century King Edward gave his Royal Assent to the Champerty Statute and for centuries afterwards champerty and maintenance were prohibited. Intermeddling for gain was out, with all its dangers – concealment of evidence, suborning witnesses,

exaggeration of loss and so the risk of real damage to the administration of justice. In England this law was eventually repealed in the 1960s. Recent decisions make it clear that the concerns relating to champertous or maintenance arrangements are to be determined according to public policy considerations such as:

- analogy to circumstances where such agreements are already lawful e.g. insolvency cases
- facilitating access to justice, and equality of arms
- the mere fact of such an agreement does not necessarily involve material prejudice to the administration of justice
- is, or was, there a material opportunity to the funder to influence the conduct of the litigation to serve his own interest as distinct from the proper running of the litigation.

[see *Factortame* (2002) EWCA Civ. 932; *Arkin* (2003) EWHC 2844 (Comm)].

So we can conclude that the use and scope of third party funding is a matter of public policy and will not be unlawful unless there is demonstrable risk, or proven occurrence, of conduct undermining the due administration of justice.

Broadly speaking I suppose this to represent the general position in the federal and most state jurisdictions in the US.

### 3. The modern objective of funding in the civil legal system.

The English Civil Justice Council in its 2005 Report “Access to Justice – funding options and proportionate costs” put the components thus:

- a meritorious case
- the participants having at the outset access to means of funding their case
- the lawyers on each side having at the outcome access to reasonable remuneration
- the costs of funding and remuneration being proportionate to what is at stake and
- the availability of an efficient and properly resourced court system.

So we can conclude none of these conflicts with responsible third party funding and claim transfer. Neither is there risk to the principles of client duty, privilege or the professional independence of lawyers – as I will develop later.

## RECENT ENGLISH AND INTERNATIONAL TRENDS

It must be noted that in England:

- the losing party pays the winner’s costs
- contingency fees are forbidden
- there are no juries in most civil trials
- there is a substantial civil legal aid system financed by general taxation
- civil legal aid is under very severe constraints

- civil litigation generally is costly
- commercial litigation is very expensive e.g. a recent intellectual property dispute in which the winner unsuccessfully claimed £5.2 million in costs for a five day hearing.

Not surprisingly there has been wide ranging reform:

- Lord Woolf's report of 1996 led to fundamental procedural changes – the three track system for small claims, fast track for modest claims and the longer term track for more complicated cases; much stronger case management control by judges; cost limits and an emphasis on alternative dispute resolution
  - the Access to Justice Act 1999 allowed conditional fee agreements where the winning party could claim costs and a success fee on those costs of up to 100%. In 2000 the law changed so that the success fee was to be paid by the loser instead of the winner himself. Defendant insurance companies engaged in a plethora of satellite litigation about such claims. Lawyers were and are attracted to these conditional fee agreements so helping the government objective of using this system to reduce legal aid and improve access to justice
  - the Civil Justice Council Report of November 2008 has opened a debate on whether we should introduce some form of contingency fee system. Only last month a preliminary report on legal costs from Lord Justice Jackson, a Court of Appeal judge, proposes radical changes to costs emphasising capping costs, proportionality and reducing the costs of commercial litigation
  - and as I have indicated our Courts have generally accepted third party funding and claim transfer.
  - And so has the High Court of Australia in the case of *Fostif* [(2006) HCA 41].
- Indeed Australia:
- repealed its champerty statute
  - has listed law firms
  - has listed litigation finance funds

Germany has no champerty law. It operates a fixed fee system for lawyers. Insurance cover for litigation costs is common with insurers such as Allianz taking from 10% to 40% of the recovery according to the nature of the claim.

## US DEVELOPMENTS

Out of deferential respect to you all I will keep this brief.

My understanding is that in federal and many state jurisdictions the US position is broadly similar to ours on third party litigation and claim transfer and the law, or previous law, of champerty and maintenance.

These issues had their modern expression in *Mississippi v. NAACP*.

There is a substantial judicial sentiment that other legal protections are a sufficient proxy for champertous concerns – the prohibition against frivolous lawsuits; the Rule 11 sanctions, and reporting lawyers in relation to ethics complaints.

More generally the “monopoly” of American lawyers to trade in claims through contingency fees requires fresh consideration – is it efficient? is it financially “literate”? how would responsible external capital funding prejudice its utility in providing access to justice?

In any event the market is already developing:

- the “open market” for transfer of patent claims, a sector said to involve outside investment of some \$4 billion
- the accepted market for claim transfer in bankruptcy proceedings where the trustee is treated as a “sophisticated seller”
- the “retail” sector for certain personal injury claims which are susceptible to monetisation techniques.

So we can conclude that the comparative perspective from our two common law worlds is that in our different ways and for some different reasons we are moving towards the same approach to third party funding and claim transfer.

#### NOTE

A most important change in English law may have profound international ramifications. The Legal Services Act 2007 permits the creation of alternative business structures for law firms. Direct investment and ownership by non-lawyers is permitted. There are safeguards:

- the professional work and conduct of the firm still has to be run by lawyers
- a complex regulatory system is being created including fitness to own criteria for investors, and recognition of the core obligations of the legal profession
- it will take until 2011/12 to become operative.

The statutory objective is to allow law firms to be capitalised, become more efficient, more competitive, and further to permit ownership by sectors such as trade unions, NGOS, charities etc.

The effects of this on cross border work, international law firms based in the UK and on professional issues of conflict of interest and confidentiality are unpredictable. As Chou en Lai said when asked to comment on the effects of the French Revolution – “it is too early to tell”.

However I propose to speculate on one aspect of alternative business structures for law firms. In my view investors who are prepared to fund, or invest in funds for, third party litigation or claim transfer will not necessarily be prepared to fund a law firm in this

new way. Obvious issues are continuity of staff and structure; wider risk exposure and more complicated exit strategies.

#### THE UTILITY OF THIRD PARTY FUNDING AND CLAIM TRANSFER

The total estimated fees in US civil litigation is \$33 billion. The present reality is that:

- the commercial clients are often not prepared to cover very large costs
- the lawyers involved cannot support the capital cost involved
- bank loans at reasonable rates of interest are off the script for the foreseeable future.

#### Business:

Prospective recoveries in cases are generally believed to be un-monetizeable, except through the unique opportunity to share risk with their lawyers through contingent fee arrangements. To make matters worse, under some accounting rules, a company's prospective recoveries in litigation (often no matter how robust the prospect of winning) cannot generally be assigned much if any value prior to an actual recovery. Such rules trap sometimes massive capital values inside "claim assets" for an indefinite time. Businesses faced with litigation liabilities confront the inability to accurately value those liabilities in merger and acquisition transactions, resulting in distortions in transaction prices – and even failed deals. The perceived inability of businesses to unlock wealth embedded in litigation opportunities and liabilities, or to turn to the marketplace for help even in valuing claims, likely distorts capital transactions, requires businesses to sit on risk, and leaves the corporate law department as a pure cost center in most corporations. In other words, businesses, like law firms, want and need access to capital markets for a variety of everyday business needs. To restrict that access is economically inefficient, if not damaging.

Business claim holders – whether a major corporation with an antitrust claim or an individual in a slip-and-fall case – have questioned the fairness of the defendant's ability to transfer risk to an insurance company before the event, while plaintiffs are left to absorb all the risk of returns on their claims until the eventual outcome. Alongside the legal profession's exclusive access to contingent fee joint ventures, one can question the economic efficiency and moral justification for promoting claim transfers to insurance companies before the event, while discouraging the transfer of a claim by a claim holder after the event. Why should an insurance company be able to take direct control of a claim through the contract right of subrogation, while a financial institution is restricted from purchasing an interest in a legitimate legal claim held by a business ?

Business is ready to share capital and costs risk.

#### Law Firms:

The ABA Journal of May reported 10,000 layoffs by law firms in the first months of 2009. This was much worse than 2008. What next?

Based largely on tradition and beliefs, lawyers still seem to suffer in their ability directly to access the power of capital markets, and law firms are unable to speak publicly and openly about their need for access to those markets. Law firm management committees wring their hands over how ethically to access money to smooth cash flows and monetize receivables within the straightjacket of competing internal partner-profit competition, pressures annually to distribute profits for income tax purposes, and professional ethics rules. Law firms that undertake contingent fee work can be likened to hapless investment bankers, seeking joint venture opportunities with no internal capital reserves and in the face of pressures to dump out cash while making fair (and forward-looking) allocations of firm resources among competing power centres within the firm. The somewhat perverse result of these pressures, dynamics and perceptions is that law firms are forced to grow inorganically in order to “manage” cash flows and fund expansions – all because operating capital, so the belief goes, must be generated internally, rather than externally.

In fact, the prohibitions on claim transfer are more perceptual than real. In most US states, champerty has been relegated to the bin of legal curios. And, while fee-splitting is still prohibited in every US state, no court has ever effectively challenged the ability of a law firm to transfer to a lender a security interest in their fee income in return for a commercial loan. After all, if the fee-splitting rules were applied to an illogical extreme, a lawyer would be prohibited from paying a non-lawyer for goods or services if the source of the payment were, originally, a legal fee. In other words, there are a variety of ways legitimately to purchase claim interests and to finance a law firm’s operations and cases even under current legal and ethical doctrines.

Lawyers are ready to share capital and costs risk.

Bank Lending:

For the foreseeable future there is no realistic prospect of banks playing a significant role in loans to law firms for litigation. The belated emphasis on careful risk assessment by banks means that they simply have not got the relevant experience to make the relevant judgments especially in commercial litigation.

There is no obvious alternative to raising capital for business or lawyers.

So we can conclude:

- business, especially through CFOs, is ready for risk sharing as to costs in funding litigation and claim transfer
- law firms cannot generally afford to finance expensive litigation into the millions of dollars.

Therefore the utility of third party funding is clear.  
But can it be made safe ?

SAFEGUARDS

Safeguards are necessary – and they are available.

1. The source of the funding

There must be good standards of fitness to invest by those in the capital market. This may come from one or more of the following:

- listing on, and compliance with the requirements of, an established exchange so providing reputational security
- consequent transparency of investment sources and the declared standards to be met.

2. Suitable bases of the funding agreement:

- clear involvement by loan, equity investment, claim transfer, and where appropriate insurance protections
- capped commitment
- a reliable case strategy
- efficient monitoring
- risk commitment by contracting lawyers and/or clients
- commitment by investor genuinely to observe all applicable ethical requirements.

3. Regulation:

At present separate regulation is neither appropriate nor necessary:

- the investor, if listed, already has to meet reasonable standards of transparency and accountability, and fitness to invest
- the lawyers involved either for the client or the investor are bound by their professional ethical requirements and bar discipline
- the accountants for all involved assess value estimates and the foundation for them in accordance with IASB or other applicable rules.

If regulation were to be considered then it must be:

- necessary to meet an identified public interest
- reasonable in its requirements
- proportionate as to its content and cost effectiveness.

So we can conclude that at this time regulation is not necessary beyond that which applies anyway.

## THE EXAMPLE OF JURIDICA

1. It is a listed company on the Alternative Investment Market of the London Stock Exchange.



Adequate information about its operation is provided through its original listing documentation, its first annual report and the AIM conditions such as Rule 26 requiring regular updated website data.

2. Its area of interest is business to business – not product liability/personal injury.
3. It covers:
  - anti trust/competition/price fixing etc. Note the recent tough enforcement policy in this area from Christine Varney of the Department of Justice, and the penalty of \$1.48 billion dollars imposed on Intel by Neelie Kroes, the EU Commissioner on Competition
  - intellectual property, particularly the patent sector
  - commercial disputes whether through courts or arbitration
  - some cases involving investor/state disputes
  - all jurisdictions but mainly the USA.
4. It employs:
  - a cutting edge underwriting system
  - effective due diligence
  - full financial analysis of all factors affecting the investment, legal, financial and overall return on investment
  - quality experts on ethics, liability, damages and enforceability
  - the best lawyers.
5. It targets:
  - the Fortune 500 companies
  - the top 200 commercial law firms
6. By prudently applying its fully paid up capital of \$175 million it deals in a tight portfolio of profitable investment. It is fifth overall in the relevant annual FT rankings for the last year – our first year,
7. Using its own top drawer lawyers Richard Fields and Tim Scrantom with a JIL Board of myself, Kermit Birchfield (previously of Shearman & Sterling and now on the Board of a large mutual trust, and Richard Battey, an accountant with PWC and Schrodgers experience we give expertise, efficacy and integrity.
8. When launched in December 2007 Juridica was described by the London Times as being involved in the creation of a “new asset class”. It is in safe hands. We will do our best to promote high standards of litigation and introduce and monitor financial

competence and planning in commercial litigation and thus foster market discipline and efficiency for the benefit of all.

## THE FUTURE

We are in the early days of the development of this initiative. The signs are positive. But we can not be sanguine. The quality and reliability of the funders are central. Some have fallen by the wayside especially in the commercial sector. Nevertheless the future should be approached with confidence. Juridica carried out a significant fund raising at its start, and a second in exceptionally difficult market circumstances this spring. This confirms the need for funding by lawyers and their clients and the willingness of investors to fund.

This form of capital investment in civil litigation will:

- improve the administration of justice through efficiency and a greater likelihood of sensible settlement before trial
- help lawyers and clients better to share the risks of expensive litigation
- enable client companies to free up capital otherwise tied up in litigation commitment
- free up lawyers from financial exigencies they cannot sustain
- thereby ensure that the core legal ethics are more effectively observed.

To do all this needs help - help from Rand and UCLA. We need research on :

- the economics of the civil legal system generally, and of business litigation in particular as it affects lawyers, clients and society
- efficiency/economy gains from third party funding and claim transfer
- the role of insurance in third party funding and claim transfer
- the risks/benefits of this proposal and the contingency fee system

In conclusion the debate centres on a specific issue: whether there can be a rational role for outside capital within law markets that does not jeopardise the core social values of professional legal independence, unfettered lawyer-client relationships, and proper administration of justice. Throughout history, these goals have been enshrined in professional ethics rules, including the fee-splitting and conflict of interest rules, as well as laws prohibiting champerty, maintenance and frivolous litigation. The central question now is whether these goals can still be served while allowing third party capital to meet the needs of law firms, businesses and plaintiffs. The answer is clearly yes not least in commercial litigation.

Leading law and economics scholars generally welcome capital access to law markets: it can level the playing field between parties to a dispute; afford additional risk-mitigation options to businesses; afford monetization options to claim holders; and help free up lawyers to operate professional services firms rather than act as financial institutions.

Let us therefore look to the development of this proposal with considerable care but studied enthusiasm. Let the lawyer respect the role of outside capital investment. Let the capital investor respect and uphold the core values of an independent legal profession.

And therefore let me come to an end!

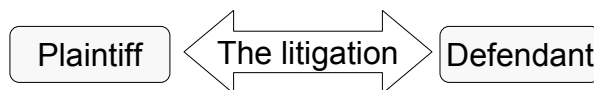


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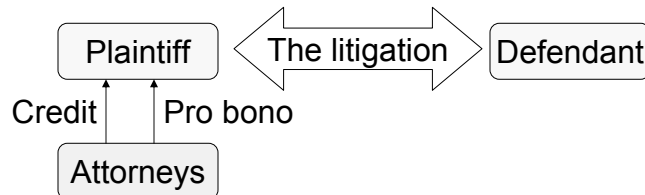
## **Framing the Central Issues**

**Lynn M. LoPucki**

### ***A Litigation-Finance Model***



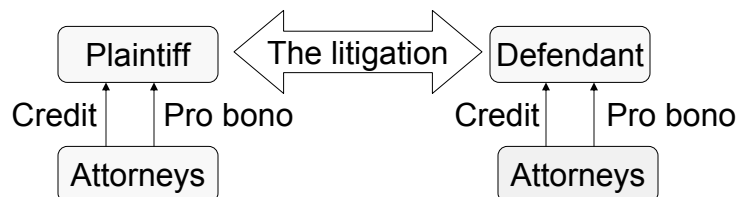
## ***A Litigation-Finance Model***



**Professor Bert Kritzer, Traditional Funding Mechanisms**

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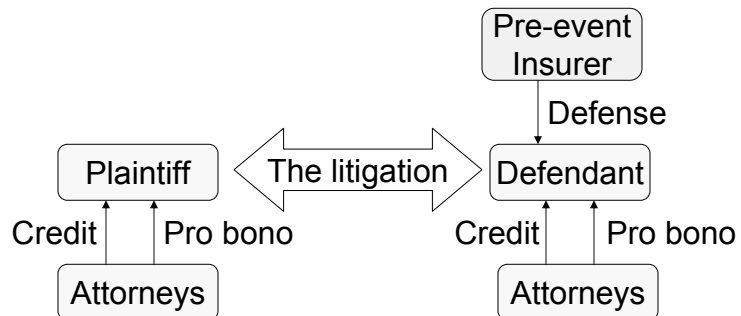
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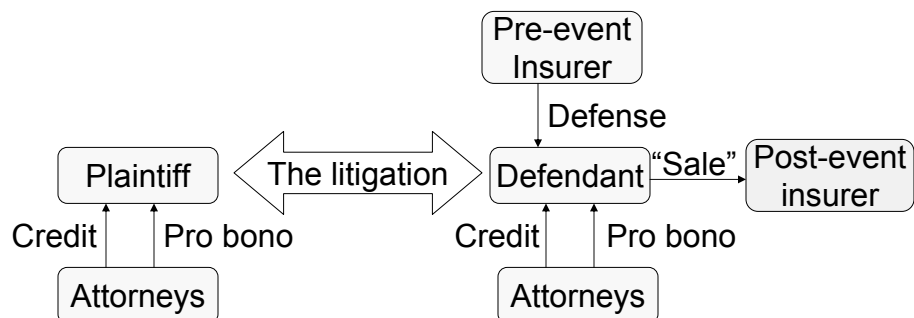
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Professor Neil Rickman, Legal expense insurance and subrogation

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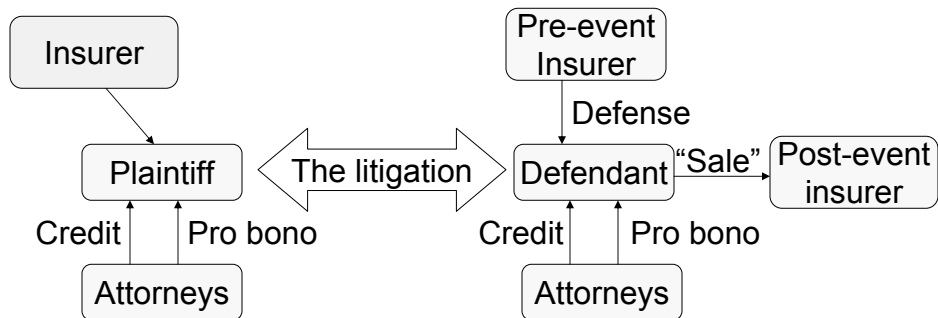
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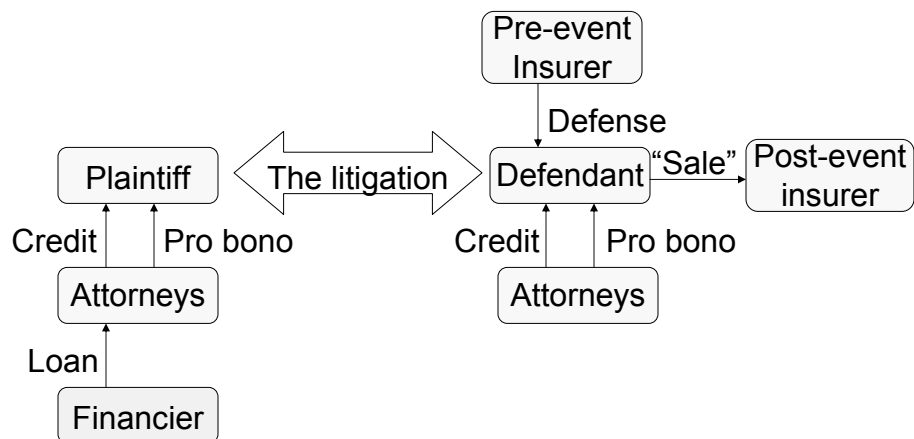
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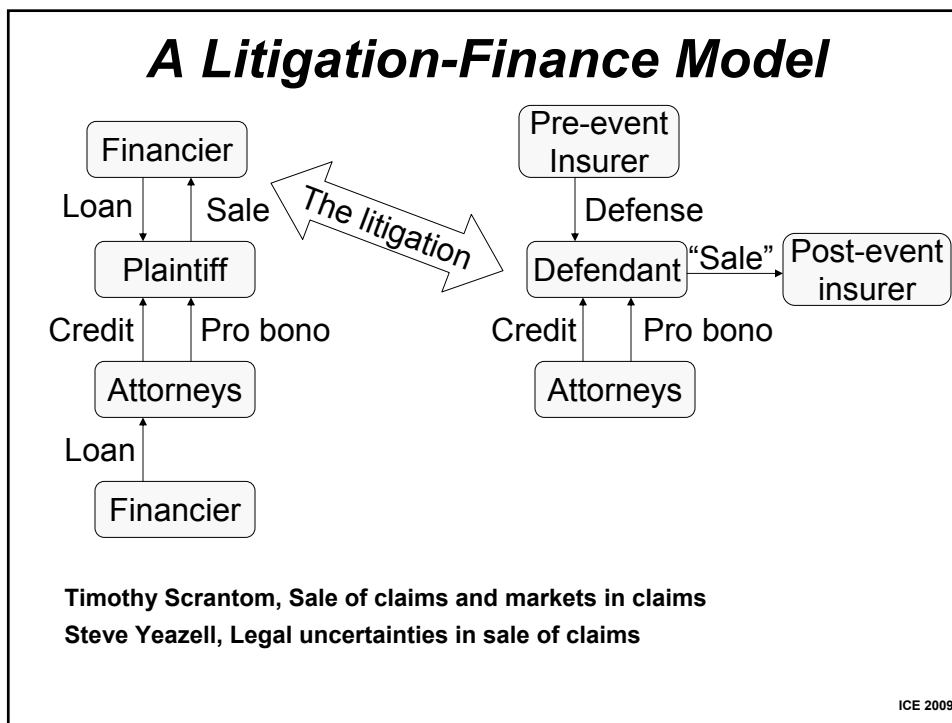
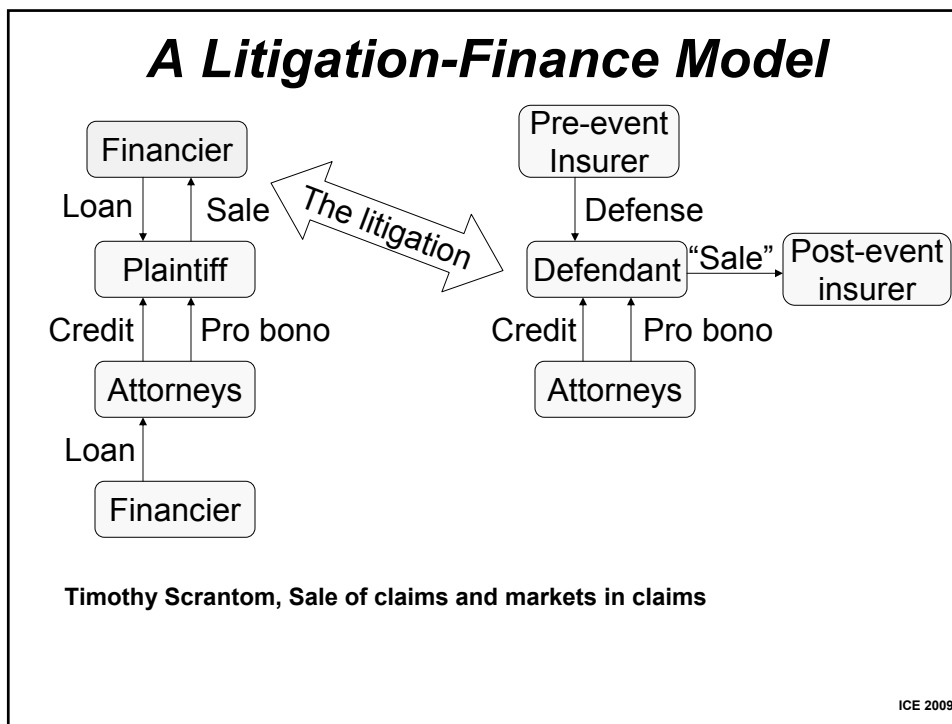
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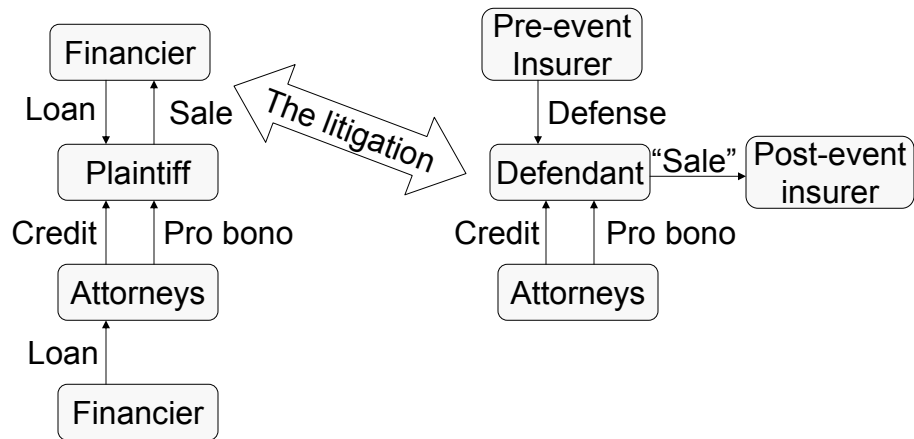
James E. Tyrrell, Financing of the attorneys

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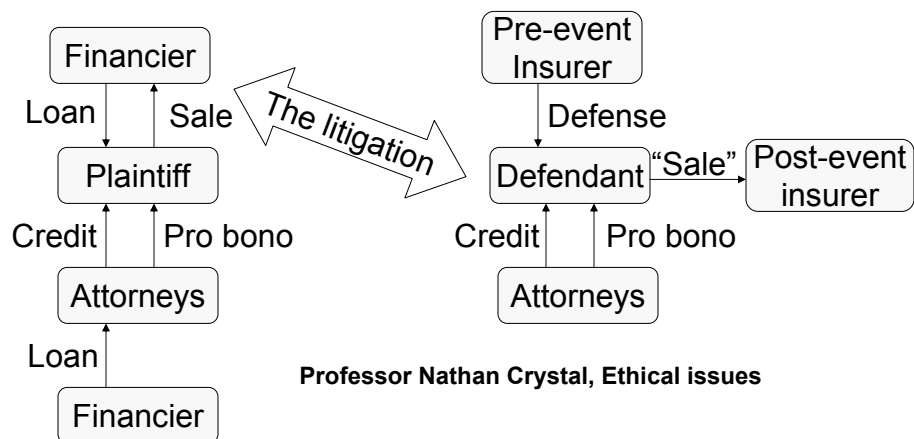
## ***A Litigation-Finance Model***



Timothy Scrantom, Sale of claims and markets in claims  
 Steve Yeazell, Legal uncertainties in sale of claims  
 Kathleen Flynn Peterson, Plaintiff evaluation of claim sale

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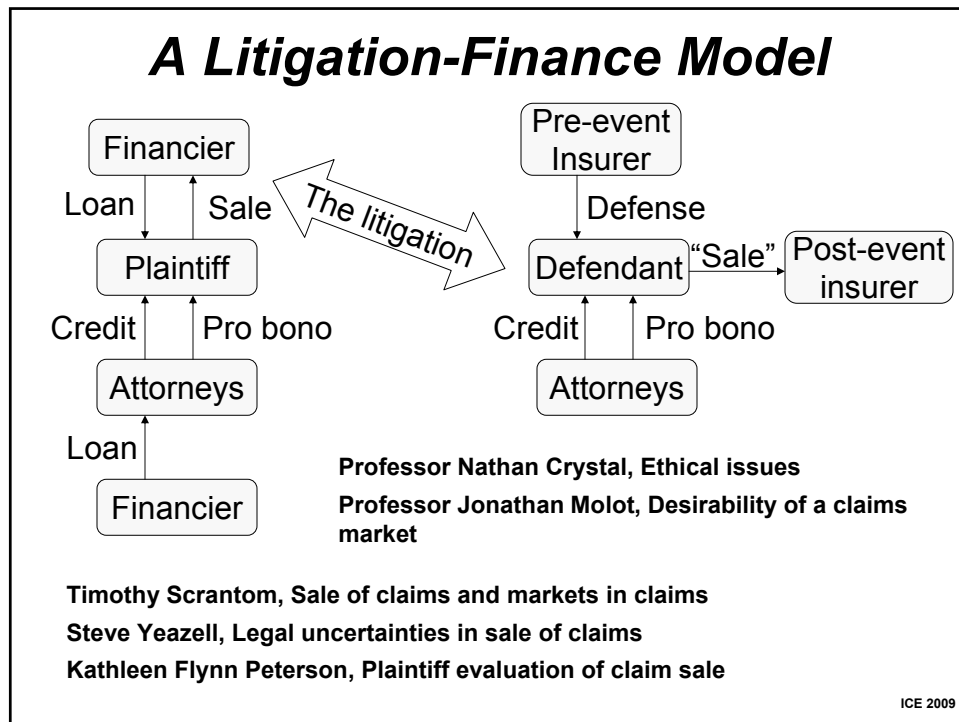
## ***A Litigation-Finance Model***



Professor Nathan Crystal, Ethical issues

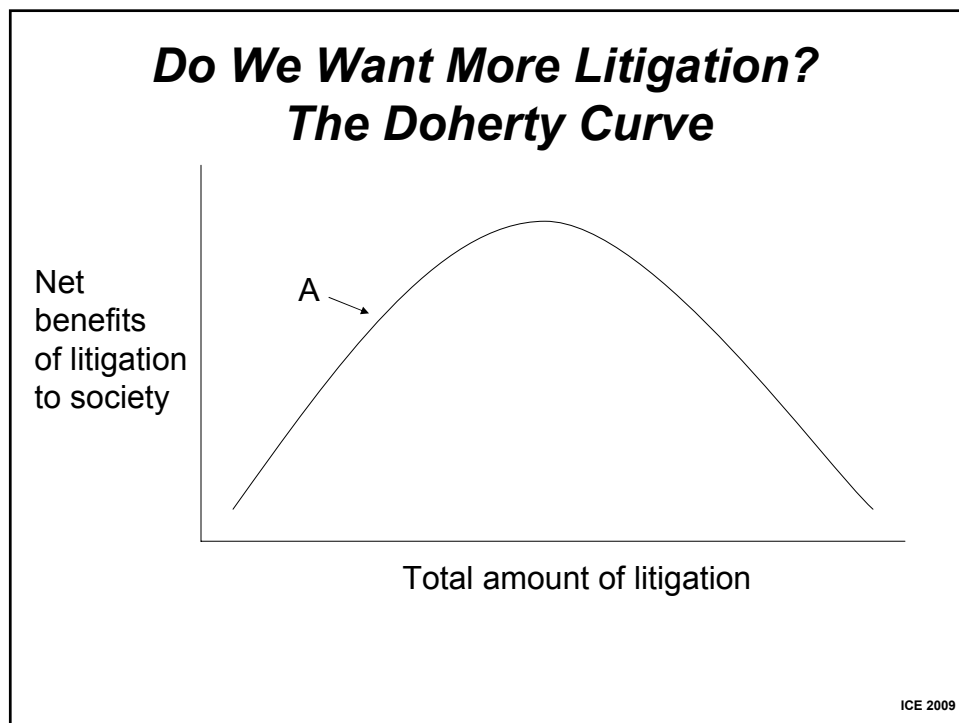
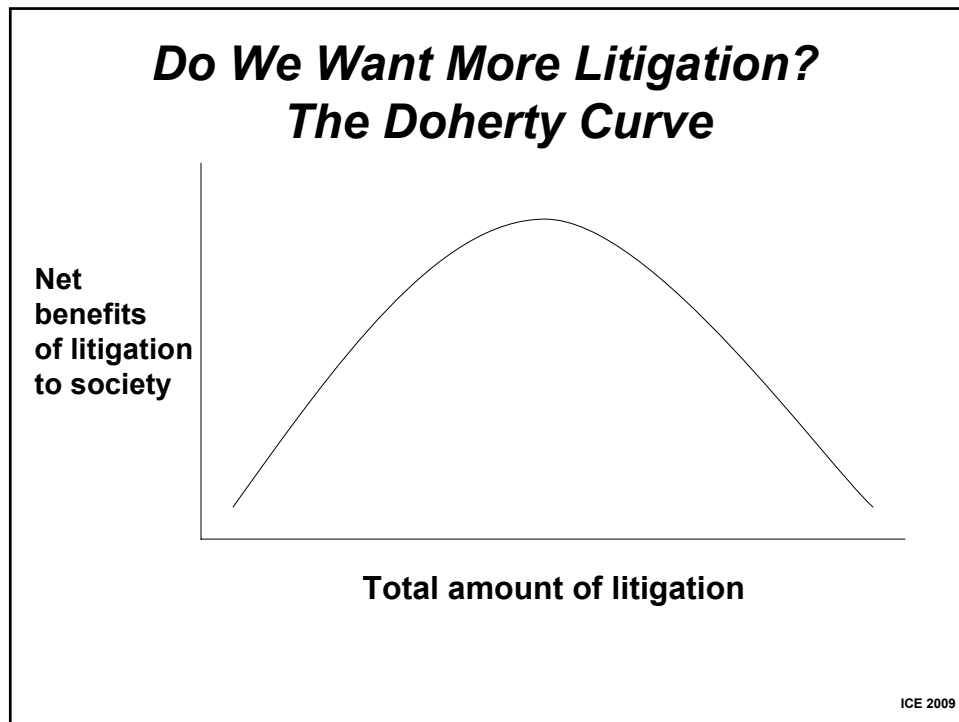
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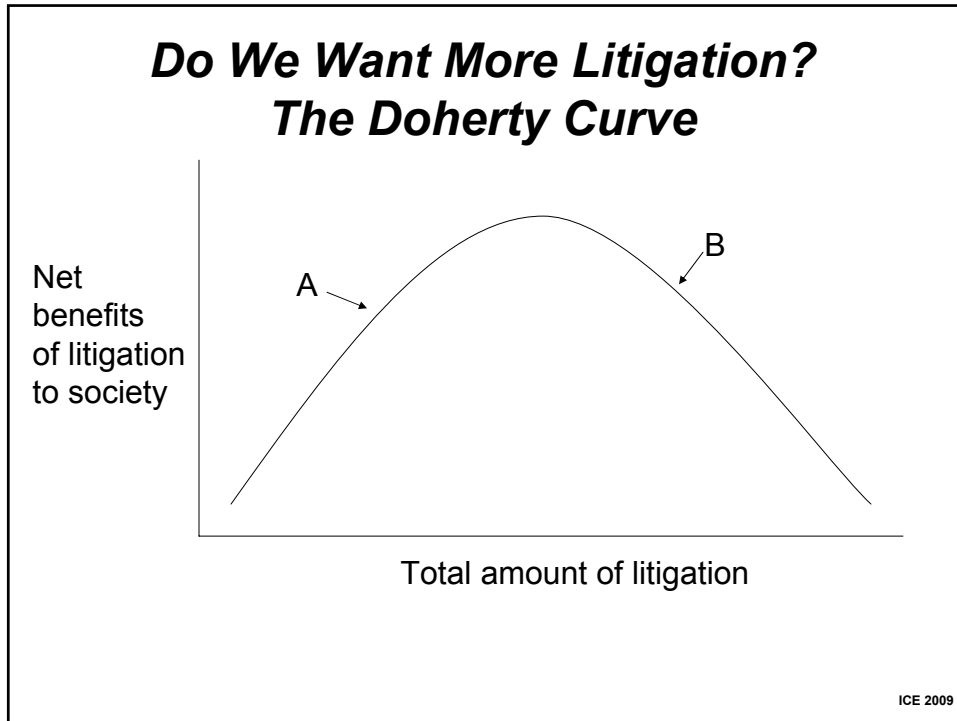
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## ***Desirability of Litigation***

1. **Deters future misconduct**
  - but over-deters, under-deters, and diluted by insurance
2. **Compensate victims**
  - but at excessive cost?
3. **Corrects injustice**
  - but inaccurately at excessive cost?
4. **Prevents the externalization of costs**
  - but also increases costs
5. **Decisions guides future conduct**
  - but court opinions, case outcomes are useless mush?
6. **Resolves disputes non-violently**
  - but is alternate dispute resolution better?





- ### ***Desirability of Litigation Financing***
1. Enables more parties to litigate, encourages disputing
    - is that a good use of resources?
  2. Levels playing field, making results more accurate
    - or just increases possibility of the expected result?
  3. Reduces the risks of litigation
    - but removes the possibility of justice?
  4. Makes claims liquid / generates “market” information
    - but removes the real parties (the empty litigant)
  5. Substitutes rational financiers for emotional litigants
    - but creates new conflicts of interest
  6. Adds parties, so adds complexity
- ICE 2009

# **THIRD PARTY LITIGATION FUNDING AND CLAIM TRANSFER: TRENDS AND IMPLICATIONS FOR THE CIVIL JUSTICE SYSTEM**

**RAND-UCLA Policy Symposium**

**An Overview**

June 2, 2009

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## THIRD PARTY LITIGATION FUNDING AND CLAIM TRANSFER: TRENDS AND IMPLICATIONS FOR THE CIVIL JUSTICE SYSTEM

### RAND-UCLA Symposium

#### An Overview<sup>1</sup>

##### A. Introduction

Today's Symposium is the first conference in the United States focused specifically on Litigation Funding industry. This industry is newly-arrived, and has had little attention, discussion or analysis. It has the earmarks, however, of a welcome addition.

At this Symposium, significant participants in the industry are lecturing. We have Funders, Claimants and potential Claimants, several lawyers who participate in various and critical ways in the market, and others. My company, Burford Advisors is an active participant in the industry.

The Symposium has two overall purposes. The first is to give a status report on where the industry stands in the United States. This involves a look back into the past and how the industry has developed elsewhere, a look at the present and how the US is likely to develop nationally and internationally, and a look at the future, to see what the industry needs and should get if it is to thrive as a commercial instrument.

The second and related purpose is to examine whether the practice delivers or detracts from civil justice. In this case, there are significant common interests and objects of commercial viability and the delivery of justice. But an industry may be profitable and not deliver justice. Does this one?

The Symposium therefore answers questions where possible, but asks questions where needed; and there is plenty of room for questions. Provoking the right questions today and in the future, and getting the right answers, is a primary goal of the Symposium.

A glaring difficulty in our undertaking is that experience in the industry is too little. The data is woefully inadequate, especially in the US. Thorough analyses have not even begun in seriousness. In addition, the practice exists in a rapidly and dramatically changing context, including the changes going on in the practice of the law firms and legal services, and the financial world.

We are not starting from scratch, however. We know that the practice has successfully existed for 20 years in Australia. We know that in the United Kingdom, it has

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<sup>1</sup> Melinda Koster, the Senior Coordinator at Burford Advisors LLC, made exceptional and invaluable contributions to this Overview. This coming year she will become a student at Stanford Law School.

existed for close to 10 years, and, according to the media, is “booming.” While there have been and continue to be issues along the way – commercial, ethical, and others – we know that the demand for financing is huge, especially in this day and age where claims have surged and credit availability and liquidity have plummeted. We also know that the United States is, by far, the jurisdiction with the largest, the most numerous, the most far flung in impact, and the most expensive, litigations in the world. The US has rich soil for the industry to take root and grow.

We know enough to expect (although not guaranty) the new industry to be a contributing one. We also know that to try to ensure this and do so in the most effective way, a lot of work lies ahead. Hopefully the Symposium and its participants – hosts, sponsors, lecturers, and audience – will begin leading the way.

This paper will provide an overview. The topic is vast, so the paper is preliminary for purposes of the Symposium. Hopefully it will, with time and further review, be developed substantially.

## **B. Overview**

### **1. The Industry**

#### *(a) The Countries.*

Two countries have had significant experience in this industry. Australia kicked things off over 20 years ago. Today, it has an established and respected presence. The United Kingdom was next. It saw the beginning of the industry about 10 years ago. Today, according to media reports, it is “exploding” and the top tier law firms are active in it or promoting it.

If we look at the UK as a useful example of what is happening in today’s world and in a jurisdiction akin to ours, we see a fair amount of activity. Over the past couple of years, the industry has witnessed a good deal of publicity and growth within the United Kingdom. Most of the largest and leading UK law firms have publicly endorsed Claim Financing, many acting as attorneys in funded cases. The press has published a number of articles describing the rapid expansion of the litigation funding market (Lind, Sofia and Claire Ruckin. “External Funding Booms as Litigators Plot Upturn.” *Legal Week*. 20 March 2008; See also Weinberger, Evan. “3rd-Party Funding Fuels European Litigation Growth.” *Law* 360. 18 November 2008). Several conferences on the subject have been given, starting in early 2008.

During this time, the industry in the UK has received thousands of applications for Funding. It has financed hundreds of claims. The Courts have increasingly supported it, although with precautions (See Mulheron, Rachael and Peter Cashman. “Third Party Funding- A Changing Landscape.” *Civil Justice Quarterly*, Issue 3. 2008. 312-341; Rose, Neil. “Drive for Transparency on Third-Party Funding.” *Law Gazette*. February 14, 2008). The

Government has studied and reported on it and seems behind it provided that certain regulations be implemented (See Lord Justice Jackson. "Civil Litigation Costs Review, Preliminary Report," May 8, 2009. Part IV, Chapter 15, pp. 160-164). The industry is itself proposing measures for self regulation (Ruckin, Claire. "UK Third-Party Funding Rules in Final Stages." *Legal Week*. July 31, 2008).

The Government and the Courts in the United Kingdom have now launched serious studies of the industry (The Government is doing this under the Legal Board established by the Ministry of Justice, and the Courts under the auspices of Lord Jackson and an assembled team). The studies seem to recognize the potential to enhance the Legal System and seem designed to determine how best to define and regulate it, rather than to outlaw it (See Lord Justice Jackson. "Civil Litigation Costs Review, Preliminary Report," May 8, 2009. Part IV, Chapter 15, pp. 160-164). The UK government passed the Legal Services Act in 2007, an important piece of legislation that has opened the door to the study and improvement of litigation funding (Legal Services Act of 2007). This Legislation allowed the Ministry of Justice to establish a Legal Services Board to study and propose changes in the UK Legal System, including in platform relating to Litigation Funding The Ministry of Justice has established that Board, now in operation (Legal Services Act of 2007). In addition, three respected Funds – Harbour Litigation Funding, IM Litigation Funding, and Allianz – are drafting self regulation rules (Ruckin, Claire. "UK Third-Party Funding Rules in Final Stages." *Legal Week*. July 31, 2008).

Several conferences on the subject have taken place in the United Kingdom in 2008 and 2009 (the first international conference, entitled "Litigation: Third Party Funding: Exploring Opportunities in the New Litigation & Arbitration Market" was held in March 2008 and another, entitled "Commercial Litigation Funding" was held in London on April 30, 2009), and more are planned for the balance of 2009 (such as one in July of 2009). Moreover, some law firms, including Herbert Smith, have held conferences for their clients and the public.

Some other scattered other jurisdictions in Europe have seen the industry begin to develop. There has been some funding activity elsewhere in Europe. Allianz Litigation Funding started and is still active in Germany. Credit Suisse is active out of Switzerland. Some other countries, like Canada, and the Netherlands, have had experience in the industry, although all countries fall far short of Australia's and the United Kingdom's experience.

*(b) Common Law.*

Not surprisingly, Australia, the United Kingdom, and the United States, are common law countries. It is there where litigation is most complicated, most expensive, and most generous in damages awarded.



(c) *International.*

The industry is especially international. Given the global expansion of businesses, technology and transportation, cross border litigations and arbitrations are extensive and growing. UK citizens, for example, are suing US defendants in US Courts. The reverse is occurring. The same cross border phenomena is occurring related to Civil Law countries. Companies in France or Germany, for example, are bringing claims in the US, and the reverse is happening as well.

(d) *Claimants and Claims.*

Claimants can be institutions, or individuals. Middle market companies seem to be most prevalent, since often they are more likely to be unable to prosecute claims. Some claimants, however, can afford to bring the suit, but choose not to, and prefer to fund.

The Claims are virtually all commercial. They can be litigation or arbitration claims. They are limitless in range. Patents, antitrust, international, insolvency and other financial distress, financial institutions in collapsing markets, institutions that are walking away from deals because of the collapsed markets, basic claims of contract/fraud/breach of fiduciary duty, all well illustrate the claims being brought.

Claimants come from all over the world to sue in the United States, and many from the United States have claims abroad.

(e) *The Funds and Their "Products".*

The serious institutional funds can almost be counted on the fingers of one hand. Juridica Investments Limited, IM Litigation Funding, Harbour Litigation Funding, Allianz, Credit Suisse, IMF Funding, Claims Funding International PLC, and Context Capital, are the more known ones.

Alongside the institutional funds, are non-institutional funds. They invest on a case by case basis. They invest separately in specific litigations, sometimes alone, sometimes with other non-institutional investors, sometimes with institutional funds in a syndicate-like group.

The Funds have a number of common features, such as basic frameworks and some common interests. But they vary enormously one to the next, like fingerprints. This is illustrated below.

Two funds are public (Juridica and IMF), the others are private. The capital invested, committed, and available, vary widely (Context Capital, for example, is apparently operating without its own capital but looks to various independent investors depending on the litigation, while Juridica has had over \$200 million put into its Fund). The size of the investments each Fund favors, varies widely, some starting in the hundreds of thousands, others in the millions (such as Juridica which favors a range of \$3 to \$10 million). Similarly the range of damages

preferred or accepted varies widely, usually in the millions. Juridica has reportedly recently committed over \$60 million to support antitrust claims of about \$8 billion.

Some funds invest in US Claims, others do not. Some favor particular practice areas like patents and insolvency, others are more general. Some do not invest in certain areas, like class actions or construction, others do. Some are open to risks, others risk adverse.

The “products” being offered by the funders are varied. There is the standard financing of estimated costs against a share of the recovery. Beyond that, there are many variations on a theme. For example, the funds advanced might include funds beyond litigation costs, but also include funds for commercial or personal use. There are funds available, usually through insurance, for responding to litigation costs imposed on a losing claimant. There are insurance funds available to insure against litigation costs for the Claimant itself, when it loses. Claimants sometimes take advantage of this, and sometimes the Funder itself takes advantage of this. (Some insurers have also what is called After the Event insurance. The insurer will in this case insure the Claimant against any fees the Claimant spends in litigating the case should the Claimant lose. A big difference from funding is that the Claimant has to foot the fees first, which is often impossible.)

On the defense side, there is a “green shoot” practice starting to grow where funders will fund the costs of the defense. In essence, the defendant transfers all risk and costs of loss to the funder, in return for a payment paid to the funder. The estimates of risk, claim value, and so on, often mirror what is happening on the Claimant’s side, but there are significant differences.

This fleet of products thus varies enormously from one funder to the next, from one insurance company to the next. The products available, the criteria used, the favored practice area targets and jurisdictions, the approval process, the prosecution process, these and more all vary from funder to funder, just like fingerprints vary from one person to the next.

#### *(f) Costs for Products.*

The costing varies widely. This is a natural result of the fact that law firms vary in cost, while others are used on a contingency or project basis. Use of insurers and others impact the price. The expected contingent share that funds charge vary significantly as well. Illustrations can be given at a wide range of percentages, such as 30%, 35%, 40%, and higher as well as lower. In many senses, it is meaningless to discuss these percentages in a vacuum. They vary depending on the strength of the case, the damages involved, the amount of investing needed, the timing of the recovery, the needs of the Claimant, to name just a few of a host of factors.

(g) *Requirements for Obtaining Funding.*

The requirements for accepting or rejecting Claims also vary substantially. That relates to many important criteria, such as: the chance of success on the merits (it is commonly reported that about a 70% chance of recovery is preferred as a general matter, but this can vary); investment and damages preferences in a project; time lines expected until recovery (one to three years would not be unusual); with return-on-investment goals being different (for example, three or four to one would not be surprising). (But see published data of IMF, indicating a far smaller return).

(h) *Considerations of Privileges and Confidentiality.*

What protection and rules apply with respect to attorney-client, work-product, and other protection doctrines needs careful attention. The rules as they apply in a funding situation must be addressed as they require something beyond the ordinary protection between a client and its attorney. They are particularly intricate in international disputes, as indicated below.

(i) *The Class Action.*

The class action has been integral to US litigations for many years. In Europe, it is beginning to develop. Its benefits to Claimants who otherwise could not prosecute a lawsuit individually, are starting to be linked to the benefit available from Funding, for a formidable union.

Funding of Class Actions requires special analysis. That is starting to be given with excellent studies by such people as Professor Deborah Hensler at Stanford University Law School, and Dr. Christopher Hodges at the Institute for Civil Justice at Oxford University. (Hensler, Deborah and Hodges, Christopher and Tulibacka, Magdalena. *The Globalization of Class Actions*. California: Sage Publications, 2009; See also Cashman, Peter and Cushman, Peter. *Class Action Law and Practice*. Annandale, Australia: Federation Press, 2007.)

(j) *The International Claim.*

International claims often bring with them an array of special issues and complications. Different legal systems, rules and policies, cultures, governments, each and together spawn deep conflicts and important differences in Claims.

To resolve such claims, it becomes important to harmonize, to the extent possible, the differences when a sovereign need not obey the rules of another sovereign: the legal systems and rules differ markedly, sometimes acutely hostile, even among similar countries; and the cultures differ in values, languages, and many other aspects.

Dealing with these claims requires special experience and skill, and intricate analysis. They cannot be lumped together with the national and regional claims.

(k) *Civil Justice Versus “Champerty and Maintenance” and Other Public Policy Issues.*

There are many known complications and challenges in the industry. They can only be illustrated here.

While Claim financing is now on the march, legal and ethical issues and public policy issues persist. Under these rules, Claim financing can be prohibited on the grounds that it involves “champerty and maintenance.” Such doctrines condemn trafficking in Claims in ways that take the Claimant’s control of the litigation away from the Claimant. They also frown on the “stirring up” of litigation Claims. These rules have been challenged and slowed the development of Litigation Funding, and have dogged it from country to country.

They have been addressed in Australia and in the UK, and it seems that they are better understood and manageable in light of the good that the industry can deliver, and the dwindling need for the doctrines in light of other protections that have been put in place. They are alive, however, and in the United States, the issue must be addressed in each State as each State has its own rules. It must be addressed in the federal courts as well.

Other public policy issues have arisen that can be considered separately from these. One is whether the funding agreement is unconscionable for the Claimant. Some relationships have been challenged and examined in the Courts in terms of what the Claimant is giving up and what it is getting.

The issues of champerty and maintenance had their own foothold in the United States that discouraged the emergence of the industry. Beyond this, each State, and the federal government, have its own specific laws and bar opinions relating to this, often varying one from the next (See Geraghty, Peter H. “Litigation Financing.” *ABA EthicSearch*. August 2006 for an overview of opinions; LA County Bar Association Formal Ethics Opinion No. 500; Florida Bar Opinion 00-3; New York Opinion 769, New York Bar Opinion 754, New York Bar Opinion 666; Texas Bar Opinion 483, Texas Bar Opinion 481, Texas Bar Opinion 465). This has complicated the analyses and slowed the process.

Nevertheless, Litigation Funding is increasingly regarded as an instrument of Civil Justice protecting Claimants with worthy Claims, a public good, rather than a mechanism for stirring up litigations for the main benefit of bystanders and commercial shysters. To many, champerty and maintenance are obsolete doctrines. This is particularly so in view of the desperate need for financing and the regulations that currently exist. Courts and rule making bodies have therefore begun to accept Claim financing, and with some increasing frequency have even praised it.

*(l) An Overriding Problem: Inadequate Information and Analysis in the Industry.*

It has to be remembered at every stage, that the industry is essentially a private one. There are only two public Funds. Moreover, the Claimants, and other participants in the industry, are not broadcasting information. Collection and publication of information has not gotten very far. There are a lot of unknowns. This fact, coupled with the relative newness of the industry, means that the information available is limited and in essence unverified.

It is also relatively unknown what contingency law firms, successful and unsuccessful, bring to the situation. How many cases they have handled, the recoveries and non-recoveries, the amount of time and effort put into cases, and so on, is not satisfactorily available.

Indeed, the litigation costs in general that are spent in the US cannot be reliably calculated. We understand from a Fulbright and Jaworski recent report that in 2005 about \$200 billion was spent on legal fees. How much of that was litigation? What was the nature of the litigations? How much was recovered? What is the breakdown for arbitrations? What are more current figures for 2007 and 2008, after a surge in litigations and arbitrations have occurred? How is the contingency world accounted for, if at all?

We do not know what these vital statistics. They are not satisfactorily available in other jurisdictions. They need to be obtained, as discussed below.

*(m) Some Tempering Factors to the Lack of Information, Analysis, and Experience in the Industry.*

While new as an industry, with a woefully short supply of information, analysis and experience, we are not completely in the dark. Litigation risk analysis has itself been around for years, illustrated below.

- contingency law firms deciding whether to take on a case have developed methods for carefully evaluating the cases that they choose to pursue; mediation of disputes.
- law firm funding firms which have loaned money to contingency law firms to provide them with cash while they pursued their contingency firms.
- due diligence evaluation of Claims against and by an entity during the sale or refinancing of the entity.
- mediations evaluating the claims and defenses.
- hedge fund analyses of major disputes that impact the value of the entity being invested in.

- entities establishing reserves against claims; auditors' analyses to determine what needs to be reflected in the financials.
- insurance companies' efforts to determine premiums to charge for insurance, or to determine how to proceed with cases they have insured.
- law firms' considerations whether to bring into the firm a litigating partner or a group of litigating partners, and seeking to analyze the value of the litigations and arbitrations that the partners might bring with them in terms of billing and related matter.
- when claims are made against an insured entity or directors and officers; banks deciding whether to extend loans to companies, individuals, or law firms who are involved in disputes.

Nor is the transfer of Claims novel. Assignments of Claims have gone on for years. The validity of the transfer has been determined by the Courts for years, even in situations dealing with whether or not a transfer is effective to create diversity jurisdiction for Federal Courts. Claims have been transferred as collateral. They have been sold outright.

Payment of fees to intermediaries in connection with the transfer of assets also has a long history. Brokers in the real estate industry are an example. Payment to those assessing equity to invest in businesses is another example. Investment bank fees are yet a third example.

Claim financing itself has existed for a long time. In essence, a contingent law firm in the United States is "financing" the legal fees of Claims by deferring the fees until and if a contingent case is resolved favorably. Sometimes, third parties pay for the anticipated out of pocket costs that contingent fees do not absorb, in return for a share of the recovery. Similarly, as noted above, third party financing parties have been financing personal injury cases for years by loaning money to the law firm prosecuting the case, and this undertaking has entailed valuing a block of cases and sometimes securing the case out of pocket expenses.

We therefore have some experience, even if some has not been on our soil, and some principles and practice, even if developed in another context and under different legal systems, to draw on. These can and need to be put to good use in the continuing study of the industry. This is discussed further below.

## **2. Important Participants in the Industry**

The Industry depends on a supporting cast for the Claimants and the Funders. They include the following

(a) *Contingency Law Firms.*

Contingency law firms play a role in the industry. They can both collaborate and compete with funders. At times, these firms team with funders to support the different activities and costs of a Claim and share the proceeds.

On the other hand, they can also replace the need for a funder by agreeing to defer or waive the claimant's legal fees in return for a share of the recovery. The slowness of the industry's appearance in the United States can partly be attributed to the fact that the contingency law practice has long been accepted here (Kritzer, Herbert M. *Risks, Reputations, and Rewards: Contingency Fee Legal Practice in the United States*. Palo Alto, California: Stanford University Press, 2004). While the limited number of quality contingency firms and the limited scope and capacity of such firms has left a serious need for the litigation funding industry and its newness still does not have the traction abroad to make it a commercial reality here.

The contingency world has its own financing industry. A number of financiers of contingency law firms have developed which lend money to contingency law firms, typically secured by a package of cases being financed and the law firm itself. E.g., Oxbridge Financial Group LLC. These businesses are generally involved with personal injury and similar non commercial claims. They are usually lenders to the mid market law firm which cannot self finance, as most of the major contingency firms can.

(b) *Law Firms in general.*

Law firms in general are central to the Funding industry. First, they are the ones that usually take the laboring oar in evaluating and prosecuting cases. A good lawyer is essential to maximize the strength and success of the claim. Second, they often assist their clients who cannot sue and do not wish to seek a contingency firm, to try to find suitable funding for the client. Here too they play a pivotal role in the industry.

(c) *Insurers.*

As obvious from the above, insurers are important to the Funding industry. They work with the Funds and supplement protection, they work apart from the Funds and directly with a Claimant or defendant.

(d) *Brokers.*

Some brokers have started to appear. They try to link Claims with Funders, insurers, and others, based on their knowledge of the industry. They are generally said to charge in the range of 5% of the recovery. There are only a few known ones, at present, notably in the UK: Calunius Capital, the Judge, and Gals. There are others that are not well known or not in public view. There will likely be a number of others appearing.

*(e) Independent Active Participants.*

There is also a need for other and independent active participants to deal with any number of aspects of the industry, whether giving independent expert consultant to claimants and to funds on such matters as evaluating or processing or prosecuting and resolving claims; forming a fund; acting with or as a fund; among a number of other activities addressing the needs the industry has. Burford Advisors is one and is comprehensive and international. Others can be found that operate in specific areas with a specific focus, but are not well known. Glenora is one. Kirk T. Harley is another. Hedge funds have retained certain litigation risk analysts to assist in certain areas. Others will be developing and become known.

### **3. Is there a market for litigation funding?**

*(a) In General.*

At the end of the commercial day, the basic question is whether there is a market for the industry that fulfills adequately a need and can operate at an acceptable profit. There is no 101 economics course concerning transferring litigation claims for value. The industry is too new. The “asset” – a claim, the value of which depends on services, with inherent special uncertainties and risks – does not lend itself easily to a conventional economic analysis.

Nonetheless, in important ways, analysis is informed by information about the purchase and sale of typical assets. One defines the general market and relevant submarkets, and then measures demand, supply, profit and loss for buyer and seller.

The market in products, such as cars, can provide an initial comparison. There is a general market for cars, and many submarkets that might be defined, such as luxury versus standard. There are any number of submarkets that might be defined, such as Mercedes and Fords. There are any number of jurisdictions that exist, whether one looks and cities, towns, States, and regions. Sellers vary in age, wealth, occupation, personality, motive to sell, and so on. Buyers are equally varied.

Demand varies from jurisdiction to jurisdiction, depending on the important determining factors such as the weather. Suppliers measure demand and produce to anticipated demand. Buyers base their decision on need (weather and use), quality, and price. Sometimes bargaining occurs, based on personalities and tactics.

Is the market in cars, however defined, a healthy one? Does it provide the seller with fair profit, say 10%? Does it provide the buyer with a fair profit, say 15 %?

Is that fair when compared to expected profits for sale of comparable products, or is it excessive and out of balance?

If excessive, what is the reason? If the reason is inadequate, what can be done to correct the profits? Is the situation a product of a temporary irregularity in the market, or



something more. Will it be fixed when the irregularity passes. Is another force needed to correct the regularity, such as by regulation by government or the courts?

While important basics can be gleaned from the market for products, the market for litigation claims is not about buying and selling typical products. Instead, it is in its essence basically a market in services. The claim needs legal and other services to prosecute it and convert it to cash. Indeed, the claim needs legal and other professional and business input to estimate "value". This takes into account the strength of the claim, the likely damages available, the enforceability of any judgment, and the cost of prosecuting the claim to conclusion.

A central end game factor in this analysis is the projection of what the settlement value is of the claim. While evaluation of all the other factors is important, this is perhaps the most important. Most disputes, by far, are settled. Over 90% of litigations are settled. A great many arbitrations are settled. The Funder usually is looking for a case that will settle well, and hopefully earlier rather than later. This is therefore an essential factor to consider.

Once the evaluations are done, the claim is put on the market. Negotiations occur with the "buyer", that is, the funder, or with two or more. Contact and negotiations may occur with one or more contingency firms. An insurance company or broker may be brought into the discussions to deal with one or more elements in the transaction, such as insuring against the possible award of legal fees to a successful defendant, or insuring and paying for the out of pocket costs of the litigation, or insuring the Funder or the Claimant directly for payment of legal fees of the Claimant if the Claim is lost, or insuring the defendant against legal fees or loss of the case. The Claimant may retain a broker or an advisor to assist in the process.

A deal is sought that can contain any number of variables in "price" and "cost". These variables relate to the form of the "purchase price", including the following forms:

- loans to pay legal fees, and perhaps something more such as commercial or personal expenses; or
- commitment to pay legal fees, and perhaps more for commercial or personal expenses.

The "sales" terms have different forms, including:

- an interest in the proceeds of recovery, or
- the equity in the company with the claim, or a portion of the equity.
- different possible terms of payment , relating to such key factors as (1) size of overall payment amount,( usually different at different stages of case); (2) timing of payments; (3) conditions to payments (including rights to terminate the agreement).

The decision on whether to “buy”, and on what terms, has multiple variables, including analysis and estimates of the:

- strength of the Claim, or likelihood of success;
- amount of the true damages;
- enforceability of the Claim;
- timing to get through trial and final judgment;
- timing and likelihood of settlement, and
- likely settlement amount.

The decision is impacted seriously by many factors and variables, concrete and subtle. They include:

- Whether or not proceedings have started, and the related stage of the proceedings and any discussions among the parties.
- Whether the case is an arbitration or a court case.
- If Arbitration, the likely panel, and special clauses that might apply such as those relating to possible discovery, and permissible evidence.
- If Court, whether the case is (or is expected to be) a jury or judge tried case, and if jury, the nature of the jury that can be expected, and if a judge, what the judge’s relevant past record is indicating the judge’s prior decisions as they relate to the issues in the case.
- The law that governs.
- The venue that may govern (with possible implications of trying a case in that venue, including cost, possible varying sympathies), and whether there is an exclusive venue clause.
- The issues.
- The discovery needed.
- The procedural and substantive motions that have been or might be made.
- Timing.
- The costs that the litigations have generated and will generate.

- The evidence expected or obtained, including the quality of the witnesses.
- The parties and the lawyers involved, and their personalities, cooperativeness, litigation styles, and quality.
- Possible settlement junctures in the process, and likelihood of settlement at the anticipated junctures.

Beyond these factors, are overriding factors when disputes are international, as many major ones are. The differences in the legal systems, laws, cultures, public policies, politics, of different countries, to name many of the important differences, can individually or collectively have an enormous impact.

Here are important illustrations of the difference in the US and UK legal systems:

- the legal system in the United States involves comprehensive and extensive discovery and enormous cost, including expensive depositions, while that in the UK has less extensive discovery, without depositions as a rule, and limited discovery as to third parties;
- typically includes juries in court cases, versus the reverse in the UK;
- does not as a rule allow the successful party to recover attorneys' fees from the loser, while the UK generally does provide for recovery of reasonable fees;
- allows full contingency cases, as opposed to the UK which only allows limited contingencies in various cases, enabling lawyers to offer legal services at less than the usual hourly rates provided they never charge more than twice those rates on a successful result;
- allows treble damages in various situations, such as antitrust cases, and punitive damages in certain serious cases, while in the UK treble damages are not allowed, nor are punitive damages a part of the system.

The substantive and procedural laws in the US are also significantly different from those in the UK in various respects. As examples:

- the anti competition laws differ, such as the allowance of treble damages for violation of them in the US, but not so in the UK,
- the laws of attorney client privilege, and work product protection, vary,
- the discovery laws, as indicated above, vary

In connection with the differences and sometimes direct conflicts in the laws, there are different ways that each country tries to harmonize them to the extent possible, through

legislation and court decisions. The venue and the countries conflicts of laws can be of central importance.

Beyond this and related to this, there are different attitudes in the UK and the US towards disputes. By way of example, the UK culture seems more inclined in general to pursue settlement, and have a stronger distaste for litigation, than the US, many have said.

Moreover, commercial litigation funding itself has different experiences in the two countries. As noted above, in the UK it has existed for about 10 years, developing more actively more recently. In the US, it is just starting with seriousness.

Within this industry, there have been varying degrees of political and legislative decisions relating to litigation funding, including fundamental issues in the ethics and public policy. In the United States, there is the extra complication that each State has its own ethics and public policy rules, and they can vary widely from one State to the next.

The industry of litigation funding, therefore, operates in significantly different environments. This can be seen in the three principal jurisdictions, the United States, the United Kingdom, and Australia. The cross-border nature of many US disputes, often has to address these differences.

The differences impact the market for claims in obvious ways, from evaluations of the strength of the claims, to the costs of prosecution, to the timing, to the likelihood of settlement, to mention some obvious and important ways.

On top of this, there is the impact that personalities play in the market. Claimants have different personalities. Some love disputes. Others are terrified by them. Some are risk adverse. Others are risk takers. The Funders themselves have different attitudes. Some look for less risk, and less reward. Others search for risks. The litany could go on almost indefinitely. This inserts an important variable into all of litigations. They play their part here.

Determining the nature of the industry is therefore not easy, let alone measuring the economics. The lack of experience, and data, and study of it, also make a comprehensive and reliable analysis of the economics impossible at this point.

Nonetheless, there are some important knowns, as noted above. We know that the Funders are seeking some acceptable recovery rate for their investments. That rate varies widely depending on the Claim and its features and the Fund and its character. That does not mean that these returns were the right returns, as today's turmoil indicates, but it is an indication that markets are prepared to recognize risks and reward them. In this industry, risks are real. A thorough analysis of what these returns have actually been, and might be, would be needed to try to pin this down more specifically.

Moreover, from limited experience in the UK and the US, it seems that those are returns that the market accepts, at least in this environment where claims have soared and

ability to pursue them has been hurt so badly. There is a strong need. And if the industry gives life to a deserving claim that otherwise had no hope, there is something to say that the economics are satisfactory and measurable to an extent, at today, and that civil justice is served as well.

*(b) The Trends.*

One important way to project where the market might end up, is to look at the trends, current and anticipated. Significant illustrations of current trends are:

- A movement exists towards regulation by Government regulation and by Self Regulatory bodies
- There is developing in the industry Brokers and Advisors, and other intermediaries to assist the process
- Attention is increasingly being given to and studies of champerty and maintenance, and public policy matters such as unconscionability, resulting in less of a problem from these doctrines
- Law firms are beginning to develop different pricing structures, such as partial and full contingencies, and project based pricing
- Important new products being developed, such as funding combined with insurance and/or contingency firm participation to some extent; funding to go beyond the cost of the litigation, but to provide cash for commercial and/or personal use, or use as collateral for loans and other security; and funding defendants
- Specializations developing within Funds in certain areas such as patents
- Claims are surging in wake of economic problems, particularly international Claims
- But Capital is being used up by the institutional funds, leaving capital and funding short falls
- Litigation cost saving practices are spreading in demand, and supply, including use of legal outsourcing and contract lawyers
- Class actions are starting to use litigation funding
- Law firms are shedding lawyers
- Claimants who can afford legal fees are starting to nevertheless turn to litigation funding for the benefits it provides

- The UK has opened the legislative door to dramatic transformations in the legal industry, including allowing under various circumstances partnerships among lawyers and others, and allowing public financing of law firm practice, including litigations
- Law and Business Schools are creating relevant courses, such as courses or programs on litigation funding, legal outsourcing, combining law and finance
- Conferences and media coverage, as well as law review articles about litigation funding, are becoming more common
- Knowledge of and credibility of litigation funding seems to be growing
- Global networks and problems will see a move towards regional and national independence
- Legal Outsourcing and contract lawyering are starting to be integrated with LF
- Conferences and Symposiums, media coverage, and other dissemination of information, raising awareness and credibility of litigation funding.

Important future trends anticipated to gain importance in the future include:

- Movements upward and downward from present levels in different active areas, reflecting more experience, more regulation, more specialization, more experience and better technology, more transparency, more competition
- Licensing Requirements
- Global collaboration, including possible international regulations
- Rational markets developing in buying and selling Claims

*(c) Conclusions.*

With experience, data, analysis, and regulation of the markets through likely licensing and other requirements, the market should become more defined, more rational prices (which in some cases may be higher, other cases lower), more acceptable.

Indeed, the more regular and rational the markets become, the less unpredictable it will become. This applies across the board. It might have a special important effect in rooting out of the dispute world some of the unpredictable personal reactions that individuals have on the Claimant and Funder side to litigation risk, and the related uncertainty it injects into the market.

Going hand - in - hand with this, is more experience; increased skill in analyzing the product, increased specialization of products which has its own impact on improving ability to

analyze the product; better technology; a better comparables market developing; more competition.

Right now there is a clear imbalance and an indisputable lack of clarity for the economics of the litigation world. The demand far exceeds the supply of capital. It is in a developing state itself. The economies are in general in a state of turmoil and imbalance. The important related industries of law and finance are dramatically changing. Whether the industry delivers Civil Justice is still a question that needs attention.

But with continued experience, more data and analysis, and a return to some surrounding stability, the industry looks like one that should not only continue, but end up becoming an important new force in the law and finance world, with benefits for the Claimant and the Funder, and other participants in the market. Indeed, will there come a time when the market is developed enough so that there can be a public market can develop in the products?

#### **4. What does the future hold?**

There is an evident need for funding and contingency work that far exceeds capacity. There is an equally evident need for more information, experience, analysis, transparency, and regulation.

Despite this, we are not operating in the dark. There has been some experience, information, and analysis. We also have experience and analysis in other areas that we can and should use here, such as in the contingency world, in the insurance work, in the brokerage world, and so on.

In light of the need and what tools we do have, there is no doubt that the industry will continue to be active in the short term. There will be a greater supply to meet the needs identified above. There will be more and healthy competition.

There will be continued study and improvement in the industry, accompanied by government, private, and court rules and regulations. It is, for sure, premature to reliably project where the industry will go in future. There seems to be an industry and market that want to become established, well run, and beneficial to the participants.

It will without doubt receive growing and important attention, study and analysis. The studies and reports going on in the UK and Australia and elsewhere will benefit the US, especially since the market is so international.

We need more facts. We need more experience. We need more analysis of what we have, and what we can obtain. We need goals and plans to get there. With these, there is a good opportunity to make the industry one that is admired and a long term one.

This Symposium, by itself, is an important step in the process of learning, and planning. It is only the beginning, however. For post-Symposium activities, there needs to be

an organized and disciplined study of the industry, with reports and proposals. What is happening in Australia and the United States can happen here. With the importance of the subject, it should happen, and the earlier the better.



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***Third Party Litigation Funding and Claim Transfer  
Policy Symposium  
June 2, 2009***

## **Fee Regimes**

**Herbert Kritzer**

### ***Lawyers' Fees Are a Perennial Topic***

- "O'er lawyers' fingers, who straight dream on fees"  
William Shakespeare, Mercutio in *Romeo and Juliet*  
(1591-1595)
- "Then 'tis like the breath of an unfee'd lawyer"  
William Shakespeare, The Fool in *King Lear* (1603-1606)
- "If lawyer's hand is fee'd, Sir, He steals your whole estate."  
John Gay, Peachum in *The Beggar's Opera* (1760)





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## Lawyers' Fees and Incentives

**Fees are a central part of the incentive structure underlying dispute resolution systems**

- **Affect how lawyers go about doing their work**
- **Affect decisions by disputants:**
  - **Whether to engage in litigation-type activities**
  - **What form of dispute resolution mechanisms to use**
  - **Whether to go to trial**
- **Hence, fees constitute a key aspect of access to justice**

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### ***Fee Regimes: A Definition***

**The structure of attorney compensation for contentious work, including litigation, arbitration, administrative adjudication, and settlement of claims in the absence of third-party processing.**

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### ***Fee Regimes: Three Dimensions***

- **Who pays the fee**
- **How fees are computed**
- **How fees are regulated and reviewed**

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### ***Who “Pays” the Fee***

- Each party pays its own
- Loser pays
  - Partial or full
- Third-party
  - Insurer (“before the event” and “after the event”)
  - Legal aid
  - Litigation funding company (“third party funders”)
- “Pro se” (“litigants in person”)
  - Individuals
  - Corporations or government (inside legal staff)
- The lawyer (*pro bono*)

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### ***How Fees Are Computed***

- Time (hourly)
- Flat/fixed
- Percentage (commission)
- Item of service (task-based)
- Value to client (value-based)
- Set by court schedule or statute
- “Per diem”
- Salary or ongoing retainer
- Mixed
  - Contingent hourly (English “conditional fee”)
  - Flat plus bonus for success
  - Reduced hourly plus bonus for success

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## ***Fee Regulation & Review***

- “Taxation” of costs in fee shifting systems
- U.S.
  - Inherent power of court
  - Statutory provisions to review contingency fees
  - Fee awards by court in class actions and one-way fee shifting
  - Bar association fee arbitration programs
- Private fee auditing
  - Insurers
  - Corporations
- What standards should govern fees?
  - Should that depend on who is paying?
  - Can fees be too *low* in some situations?

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## ***Fee Regimes and Worlds of Litigation***

- Routine litigation
  - Modest to moderate amounts at stake
- High value litigation involving individualized claims
  - Medical malpractice
  - Major permanent disability
- Large scale litigation
  - “Bet-your-company” cases
  - Class actions
  - Mass torts

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## ***Elements of Fee Regimes Interact***

- **How to combine a percentage fee with fee shifting?**
  - How should one bear the downside risk?
  - How should the shifted fee be computed?
- **Under a system of legal aid, who should bear the winner's cost if the legally-aided party loses?**
  - How does that affect incentives?
- **How should fee shifting work for salaried counsel (in-house corporate or government)?**
  - On what basis should a fee shift be computed?

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## ***Fee Regimes Create Incentives***

- **Fee regimes affect value of cases**
- **Fee regimes create incentives for litigants**
  - Whether to litigate depends on who is paying litigation costs
  - When or whether to settle is affected by fee structures
- **Fee regimes create incentives for lawyers**
  - What cases to handle
  - What advice to give
  - How to handle cases (motivation for efficiency)
  - Incentives to “win”

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### ***Fee Regimes Create Conflicts***

- **Every fee arrangement has potential for conflicts**
- **Nature and degree of conflicts depend on whether one takes a short run or long run perspective**
- **Clients differ in their ability to monitor lawyers' activities with an eye to ameliorating conflicts**
  - Individuals
  - Corporations
  - Class members
- **Classic principal-agent problem**

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### ***Fee Regimes Are Deeply Embedded***

- **Expectations of participants (lawyers, litigants, and adjudicators)**
- **Procedural rules are created with the fee regime in mind**
  - “Payment into court”
  - Formalized offers to settle and differing standards for fee computation
- **Can make it difficult to think outside the box**
  - Unbundling insurance to separate coverage for litigation and for the potential loss itself

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## ***Conclusion: Thinking In Terms of Fee Regimes Reveals the Complexities***

- **Embedded nature of fee regimes makes change tricky**
  - Importing some aspects without importing others
  - Unanticipated consequences of making success fees and insurance costs shiftable
- **Thinking about one element without taking into account others is a dangerous business**
  - Can a flat fee system work with fee shifting?
- **Complexities make predicting effects very difficult**
- **Central challenge: designing pre-change inquiries that adequately anticipate the effects beyond those specifically intended**



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## **Insurance and Litigation Funding**

**Neil Rickman**

### ***Why Look at Insurance?***

- Insurance plays a high profile role in litigation
- Arguably, it provides one possible 'bridge' between the traditional landscape and claim transfer models
- When looking ahead to the future for third party litigation funding and claim transfer, it is important to be aware of this competitor, or complementary, product
  - Especially in Europe



## ***Insurers' Funding Roles***

- Provide insurance cover against legal expenses for plaintiff or defendant
  - Before the event
  - After the event
  - Particularly common in Europe
- Provide financing for claims
  - Before payout
    - To assist with contractual obligation to minimise losses (by litigating the claim)
      - Plaintiff and defendant
      - Often on terms written into the policy
  - After payout
    - Subrogation
      - Plaintiff
      - Subrogation attorneys

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## ***Subrogation***

- When a party (insurer) assumes control of the claim in order to regain damages it has paid out under an insurance contract
  - Effectively, the claim is transferred to the insurer, who funds the litigation and receives the relevant (net) damages
    - Could fund by variety of traditional methods, depending on risks, relationship with attorneys involved
  - Potential moral hazard problem can be reduced by
    - Insured's concern for loss record
    - Need to litigate over uninsured losses and deductible
    - Sub-poena (Not ideal)

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### ***Observations for Third Party Funding***

- Insurers could complement third party funding
  - Investing in funding pool
  - Providing after the event costs insurance in cost-shifting jurisdictions
- Insurance could compete with third party funding
  - After the event policies could offer an alternative funding method
    - Intermediaries are beginning to offer tailored after the event policies
  - Arguably hindered by information asymmetry and uncompetitive premiums
    - But evidence from England and Wales suggests that this market can develop in areas with reasonably large claims (medical malpractice)
    - Future developments (such as multi-disciplinary practices in England and Wales) could integrate law and insurance

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### ***Observations for Third Party Funding***

- There is important research to be done on the comparative merits of after the event insurance and third party litigation funding

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## ***Some Evidence***

- In England and Wales, legal aid has been withdrawn from most types of PI case
- Popular replacements have been
  - Before the event insurance
  - Conditional fees (CF), with ATE policies to cover costs in event of loss
- Medical malpractice is an exception: legal aid remained
  - The CF + ATE market was slow to enter here
    - Unpredictable, high damage claims
    - Costly research may reveal that there is no case
  - But it has gradually developed
    - Not least by becoming better at selecting 'safer' risks
  - Fenn, Gray & Rickman (1999), Fenn, Gray, Rickman & Mansur (2005)
    - Growing use of CF + ATE
    - But these claims tend to be less 'risky' ones

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## ***Use of CF + ATE in UK Med Mal***

Year of notification	Non- CF/ATE	CF+ ATE	Total
1995	1,336 <i>100</i>	0 <i>0</i>	1,336 <i>100</i>
1996	2,957 <i>100</i>	4 <i>0</i>	2,961 <i>100</i>
1997	4,081 <i>99</i>	33 <i>1</i>	4,114 <i>100</i>
1998	4,955 <i>98</i>	81 <i>2</i>	5,036 <i>100</i>
1999	5,203 <i>96</i>	194 <i>4</i>	5,397 <i>100</i>
2000	5,496 <i>93</i>	389 <i>7</i>	5,885 <i>100</i>
2001	5,625 <i>92</i>	515 <i>8</i>	6,140 <i>100</i>
2002	5,056 <i>92</i>	435 <i>8</i>	5,491 <i>100</i>
2003	3,402 <i>93</i>	241 <i>7</i>	3,643 <i>100</i>
<b>Total</b>	38,111 <i>95</i>	1,892 <i>5</i>	40,003 <i>100</i>

•Note: These figures will be an underestimate

•Source: Fenn, Gray, Rickman & Mansur (2005)

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### ***Preliminary Assessments of Case Prospects***

<b>Probability</b>	<b>Non- CF/ATE</b>	<b>CF + ATE</b>	<b>Total</b>
Certain (>94%)	32.0	48.5	32.8
High (75-94%)	18.9	21.1	19.0
Medium (25-75)	9.2	2.6	8.9
Low (1-25%)	25.4	20.0	25.1
Minimal (<10)	14.4	7.7	14.1
<b>Total</b>	<b>100.0</b>	<b>100.0</b>	<b>100.0</b>

Source: Fenn, Gray, Rickman & Mansur (2005)

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## LAWYER INVESTMENTS IN CLAIMS

James E. Tyrrell, Jr.

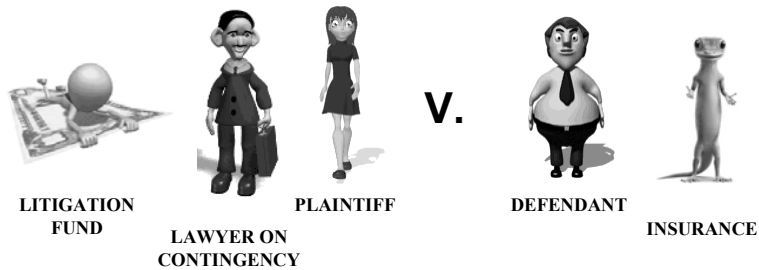
Regional Managing Partner, Patton Boggs LLP

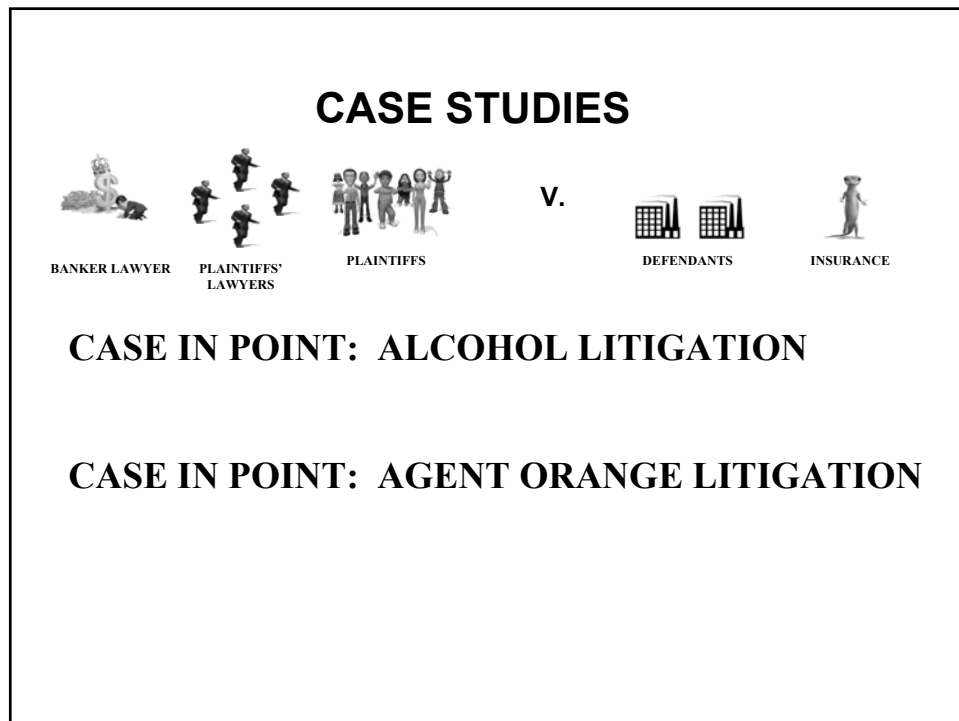
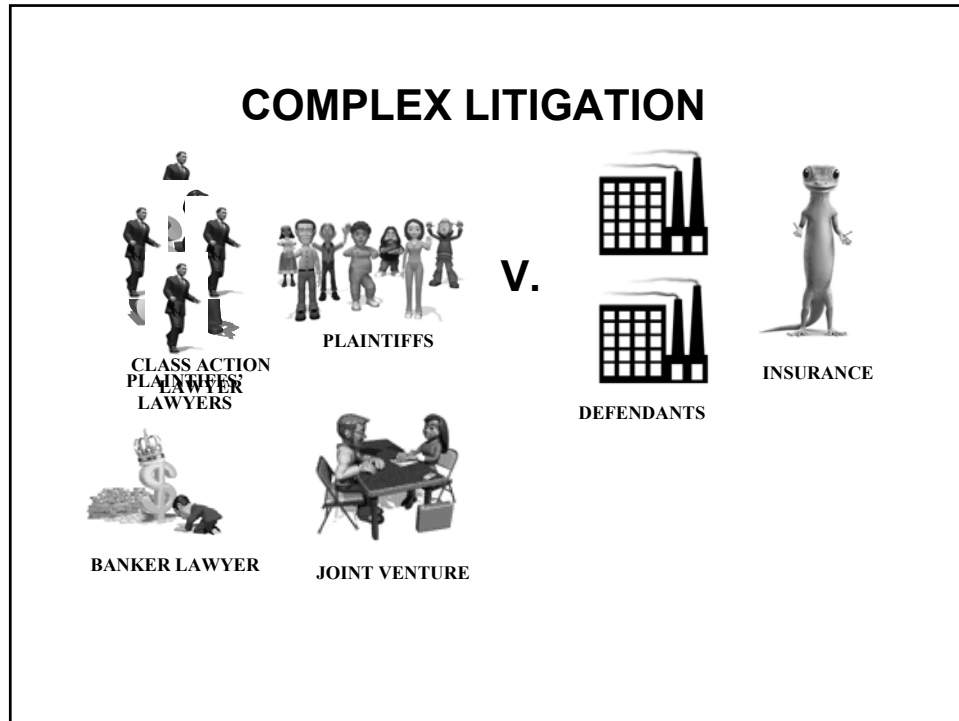
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## CLASSIC LITIGATION





## CASE STUDIES



**CASE IN POINT: Y2K LITIGATION**

**CASE IN POINT: 9/11 LITIGATION**

## IMBALANCE OF RESOURCES



**LEADS TO OPPORTUNITY**

## **The Future: Defense Funding**

### **Defendants + Counsel + Upside**

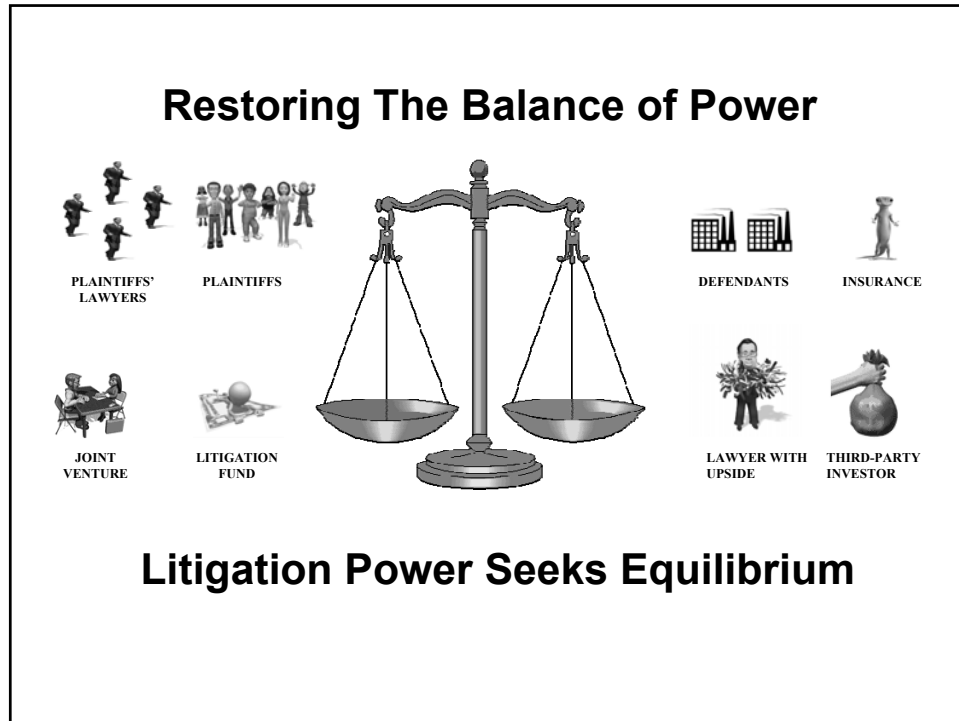
- Examples:
  - Incentive Based Legal Services
    - Summary Judgment Motions
  - Contingent Defense
    - Failing Company
      - Trading Equity For Legal Services

## **Third-Party Defense Funding**

### **Defendants + Counsel + Upside + Investor**

- Examples:
  - Block Injunction
    - Partial (or full) Contingency
    - Percentage of Continuing Sales/Profits
  - Damages Minimization
    - Sliding Scale Recovery
    - Defense Verdict Recovery





  
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**LAWYER INVESTMENTS IN CLAIMS**

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## **Sources and Structures of Claim Investments**

**Timothy D. Scrantom**

### ***Outline of Presentation***

- Who and where are the investors, what are they doing, and why are they doing it the way they are?
- Where and who are the market participants?
- How do market participants choose the investment structure?
- What transaction structures are used to invest in claims?
- Direct purchases of claim-holders and property with embedded claims
- Recourse and non-recourse loans

## ***Outline of Presentation (continued)***

- Recourse and non-recourse loans
- Purchases of choses in action
- Hybrid structures
- Derivatives
- Insurance structures
- Summary

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## ***Where are the Investors?***

- Observation: *The US is Largest and Most Sophisticated Litigation Financing and Claims Transfer Market*
- Structural reasons
  - Market size
  - Large amount of litigation
  - Ingrained understanding of contingent claim transfer (albeit to lawyers)
  - Entrepreneurial spirit (even in law)

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## ***Where are the Investors? (continued)***

- **Functional reasons**
  - **Jury role in civil cases**
  - **Substantial size of awards**
  - **Special damages (treble and punitive)**
  - **Special litigation regimes (class actions)**

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## ***Dynamics of the US Claims Investment Market***

- **“Open market” for transfer of patent claims (Federal Preemption Doctrine)**
- **Accepted market for transfer of claims in bankruptcy proceedings (trustee is “sophisticated seller”; creditors have pre-existing rights)**
- **Considerable development of “retail market” for certain personal injury claim monetization techniques**
- **Several major players in the marketplace (particularly in IP space)**
- **Major US law firms recognizing ability to finance expansion through non-traditional capital sources**
- **US-based Am Law 50 “Attention to Developments in the UK” (non-lawyer capital investment in law firms)**

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## ***Market Participation Abroad***

- The United Kingdom
- Europe
- Australia
- International Arbitration

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## ***Who are Law Market Capital Participants?***

- Lawyers
- Banks
- Retail
- Commercial
- Ad hoc investors (funds, HNWI's and institutional investors)
- Insurance companies
- Brokerage/agents/intermediaries
  
- *How much* has been invested?

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### ***Capital Flows into the Claim Investment Marketplace***

- Why is capital entering the law marketplace?
- Access to justice
- Law firm capital demands
- Complete or partial alternative to contingent fees
- Early monetization of claim asset for working capital or living expenses
- Pure hedge against risk of pursuing an asset of speculative value
- Potential to securitize a non-traditional asset class

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### ***Capital Flows into the Claim Investment Marketplace***

- Economic drivers and inhibitors to law market capital flows
  - Drivers
  - Marketplace demand
    - The anachronistic economic model of law firms
    - Innovation: sophistication of corporate legal departments
    - The desire for corporate risk mitigation
  - Supply side opportunity
    - The “non-correlated investment” phenomenon
    - The “recession-proof” business model
    - The “counter-cyclical” nature of claim finance space
  - Market size: possibility of massive capital absorption

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## ***Capital Flows into the Claim Investment Marketplace (continued)***

- **Inhibitors**
  - Perceptions, mythologies and prejudices
  - The guild anachronism in the legal profession
  - The fear of perceptions: one investment bank's experience

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## ***Determinants of Investment Structure***

- **Claimholder needs and desires**
- **Investor needs and restrictions**
- **Control issues**
- **Legal restrictions (champerty, usury, limitations on assignability)**
- **Security (recourse/non-recourse; secured/unsecured)**
- **Tax**

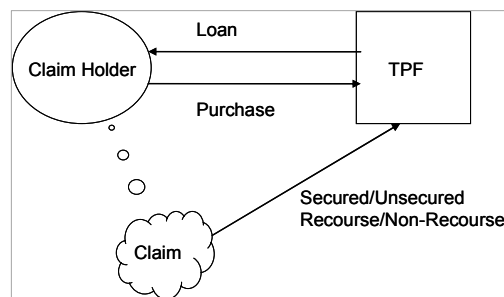
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## ***Capital Flows into the Claims Investment Marketplace***

- How is capital entering the law marketplace?
  - 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

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## ***Direct Purchase or Loan***

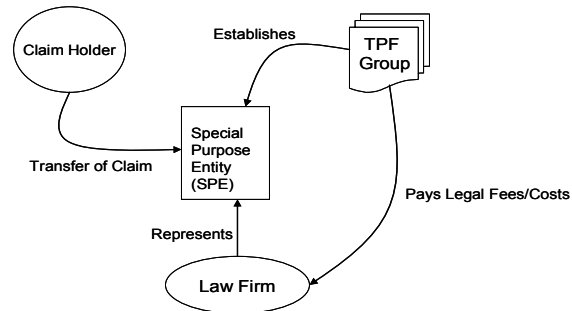


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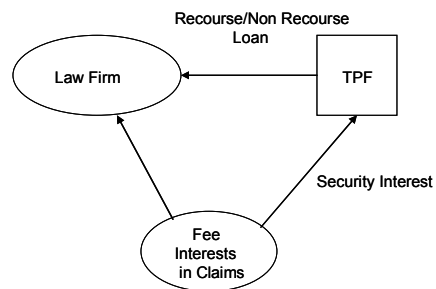
## ***Syndicated/Participated Indirect Purchase***

- **Bankruptcy**
- **Remove Claim in Merger**
- **Purchase of Patent Interest/Claim**



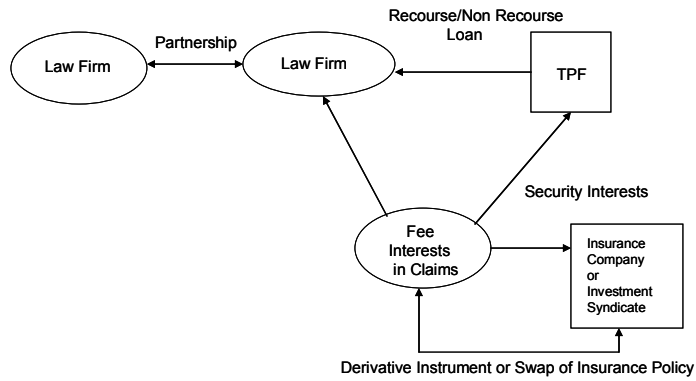
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## ***Simple Law Firm Loan***



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## ***Complex Law Firm Facility***



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## **Litigation Markets and Litigation Accuracy**

**Jonathan Molot**

### ***Outline***

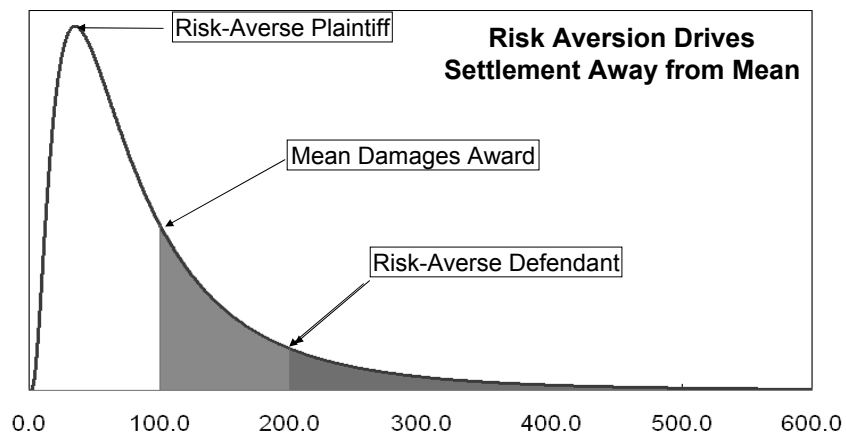
- **Litigation Accuracy and Litigant Risk**
- **Imbalances in Risk Preferences Can Skew Settlements**
- **Examples Where a Solution is Needed**
- **A Market Solution to Risk Imbalances**
- **How Diversification Reduces Risk**
- **Existing and Emerging Markets**
- **Obstacles and Solutions**

## ***Litigation Accuracy and Litigant Risk***

- Litigation system relies on settlement to replicate trial outcomes
  - Vast majority of cases settle, so accuracy of settlements is crucial to the success of our civil justice system
- If parties settle based on non-merits factors, our system fails
  - Defendant may get off too easily by convincing a plaintiff to accept too little
  - Plaintiff may extract unduly high settlement from defendant
  - Either way, the litigation system does not achieve its goals
- Settlements are a product of parties' risk preferences
  - Parties choosing between a certain outcome and an uncertain outcome will be guided by their risk preferences

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## ***Imbalances in Risk Preferences Can Skew Settlements***



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### ***Examples Where A Solution is Needed***

- **Where a lawsuit pits a one-time plaintiff against a repeat-player defendant, imbalance in risk preferences favors defendant**
  - Risk-averse plaintiff has incentive to settle at lower vs. higher median or mode expected damages award
  - Example: Patent litigation between start-up plaintiff and repeat-player defendant
- **In other instances, risk imbalances work in opposite direction – strongly favoring plaintiffs over defendants**
  - Large consumer class action lawsuit; litigation interfering with merger/acquisition

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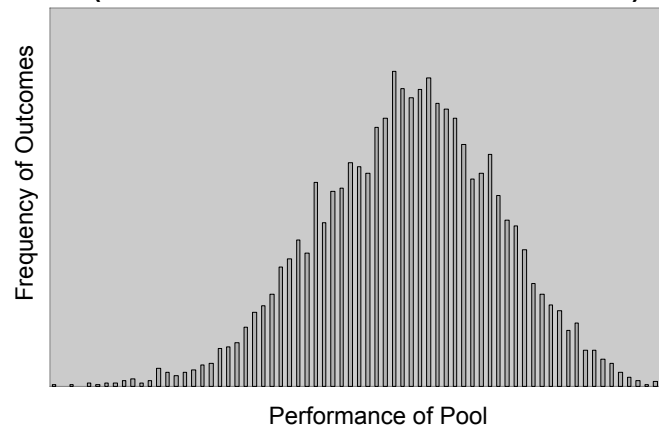
### ***A Market Solution to Risk Imbalances***

- **Mispricing of litigation settlements is just as much a market failure as a judicial failure**
  - Scholars view inaccuracy as a procedural problem and rely on judges to make settlements look more like adjudications
  - Market alternative to judicial intervention may be superior
- **Introducing repeat-player, risk-neutral entity on the side of the more risk-averse party has two benefits**
  - Promotes accurate deterrence – ensures defendants pay amounts closer to mean expected damages award at trial
  - Promotes accurate compensation
- **No longer forced to deal with a single counterparty, even a risk-averse litigant could shop claim around for best offer possible for fair recovery**
  - In a free market for litigation claims, a market participant in litigation claims would be subject to market forces that do not constrain litigants today

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## ***How Diversification Reduces Risk***

**Volatility of Performance is Relatively Low  
for Pool of Lawsuits  
(40 Suits Accumulated over Five Years)**



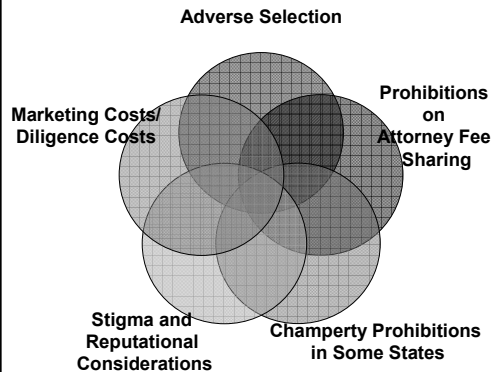
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## ***Existing and Emerging Markets***

- The contingent fee system
  - Benefits
    - Widespread and relatively efficient for some types of suits
  - Weaknesses
    - Inadequate competition from hourly fee firms
    - Lack of capital/expertise for certain types of cases
    - Inability to buy claims outright
- Emerging markets in litigation risk
  - Cash advance industry for personal injury victims
  - Fund investment in commercial litigation
  - Law firm finance

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## ***Obstacles and Solutions***



- Careful structuring to comply with prohibitions on fee sharing and champerty
- Broad relationships with law firms and careful diligence to address adverse selection problem
- Top-flight lawyers with strong contacts in legal and financial world to make sure diligence and marketing is effective
- Bring litigation finance out of the shadows and into the mainstream to erase stigma, promote competition, and expand market



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## **Third Party Finance: Legal Risk & Its Implications**

**Stephen C. Yeazell**

### ***Three Tiers of Questions***

- **1<sup>st</sup> Tier: Is third-party finance lawful?**
- **2<sup>nd</sup> Tier: How will uncertainty about the 1<sup>st</sup> tier question affect litigation?**
- **3<sup>rd</sup> Tier: If it is lawful, how will it affect litigation tactics & strategy, structure of bar?**



## ***Is it Lawful?***

- **Champerty, maintenance, usury**
  - In spite of occasional judicial eruptions, probably not a major challenge
  - But: uncertainty
- **A new bogey-man: is third-party finance a federal crime?**

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## ***What Do These Men Have in Common?***



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## ***18 U.S.C. §1346***

### **§ 1346. Definition of "scheme or artifice to defraud"**

**For the purposes of this chapter [which creates federal criminal penalties for wire fraud], the term "scheme or artifice to defraud" includes a scheme or artifice to deprive another of the intangible right of honest services.**

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## ***§1346 and Legal Ethics***

- **Some federal prosecutors have taken the position that breaches of professional ethics in various fields deprive clients of "honest services" and thus constitute federal crimes**
  - **Wm. Lerach, a theretofore successful securities lawyer convicted under this provision.**
  - **Cardinal Mahoney currently under grand jury investigation under this provision for actions in supervising priests guilty of sexual predation**

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### ***The 2<sup>nd</sup> Tier: Effects of Uncertainty***

- Will uncertainty cause firms or clients to be unwilling to finance?
  - Will uncertainty compel disclosure to clients?
  - Will clients decline to consent after disclosure?
- Will uncertainty create satellite litigation?
  - Will financing be discoverable?
    - If unlawful (see 1343), not privileged
  - Could a defendant argue for dismissal on grounds that the lawsuit itself was the product of a criminal conspiracy?
  - Could an unsuccessful client sue for malpractice on the grounds that the financing scheme created wrong incentives for lawyer?

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### ***2<sup>nd</sup>-Tier Solutions***

- What process of clarification would clarify the legality of third-party financing?
  - Federal legislation very unlikely; the 50-state problem
  - Case by case adjudication will produce long period of uncertainty
  - If legality under federal law depends on ethical standards, would clarification by state bars be effective?
    - Could a lawyer get clearance from a state bar?

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### ***3<sup>rd</sup> Tier Questions: Litigation Strategy & Bar Structure***

- Strategic
- At present, the adversaries have only their own evaluations of merits to go on.
- Will third-party financing change strategy of lawsuits?
  - Disclosing financing vouches for credibility of claim
  - Makes plaintiffs parallel with defendants whose insurers are implicitly vouching for the credibility of the defense.
- Structure of Bar
- At present only large practice organization can finance some suits
- Will third-party financing make smaller organizations competitive with such firms?
- Will third party financing serve as signal to other lenders, other clients?



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## **Professional Ethical Issues in Third Party Litigation Financing**

**Nathan M. Crystal**

### ***Transaction Structures***

**Third party financing of litigation can occur in a variety of ways:**

- 1. Purchase by or assignment to financing entity of portion of claim**
- 2. Loan by financing entity to owner of claim**
- 3. Loan by financing entity to attorneys representing claimant**
- 4. Cocounsel between attorneys who represent claimant and counsel funded by financing entity**

### ***Purchase or Assignment of Interest***

- **Financing can involve purchase of portion of cause of action or assignment of percentage of proceeds of judgment or settlement depending on local law regarding transfers of causes of action.**

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### ***Loan to Owner of Claim for All or Portion of Expenses of Litigation***

- **Types of Expenses:**
  - **Expert witness fees**
  - **Costs of document examination**
  - **Portion of legal fees if not pure contingency fee case**
- **Interest rate set by negotiation based on degree of risk owner and financing party are willing to assume, subject to any usury restrictions**
- **Loan can be recourse or nonrecourse, but for clients who wish to reduce risk, nonrecourse likely to be more attractive**

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### ***Loan to Law Firm for All or Portion of Expenses of Case***

- Types of expenses, interest rate, and liability on debt are similar to transaction in which loan is made to client

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### ***Cocounsel Relationship with Firm Funded by Financing Entity***

- If local law unfavorable for direct purchase and if loan structure is undesirable, it may be possible to structure cocounsel relationship between attorney for client and firm funded by financing entity.

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## ***Legal and Ethical Issues***

- Depending on transaction structure, litigation finance can raise a variety of legal and ethical issues
- Legal issues (discussed by other presenters)
  - Champerty, barratry, maintenance
  - Usury
  - Public policy
- Major ethical issues
  - Confidentiality
  - Fee splitting with nonlawyers
  - Interference with independent professional judgment

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## ***Confidentiality***

- Financing entities will require information about the case initially to evaluate whether to make the investment and during case to monitor and protect their investment
- Consensual Disclosure of Confidential Information
  - To obtain financing owner of claim may provide information about case to financing entity
  - Attorney for client may provide confidential information with informed client consent. ABA Model Rule 1.6(a)

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## ***Does Disclosure of Information Jeopardize Attorney-Client Privilege?***

- Elements of privilege will vary depending on jurisdiction
- Restatement (Third) of the Law Governing Lawyers §68 (2000) provides following elements for attorney-client privilege to apply:
  - a communication
  - made between privileged persons
  - in confidence
  - for the purpose of obtaining or providing legal assistance for the client

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## ***Does Disclosure of Information Jeopardize Attorney-Client Privilege?***

- Problems with maintaining protection of attorney-client privilege:
  - Is communication of information to financing entity between privileged persons?
  - Is communication for purpose of obtaining or providing legal assistance?
- Possible that privilege could be protected
- Attorneys for financing entity could be designated as agent of client for purpose of receiving confidential information
- Counsel for financing entity could have attorney-client relationship with client for purpose of case evaluation, and disclosure could be in confidence for purpose of legal advice

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## ***Application of Work Product Doctrine***

- **Federal Rule of Civil Procedure 26(b)(3):**
  - Information obtained or prepared in anticipation of litigation is not subject to discovery unless party seeking information shows substantial need for information and inability to obtain information without undue burden
- **Disclosure of information to financing entity should not amount to waiver of work product privilege**
- **Restatement (Third) of the Law Governing Lawyers §91 provides:**
  - “Work-product immunity is waived if the client, the client's lawyer, or another authorized agent of the client: . . .
  - (4) discloses the material to third persons in circumstances in which there is a significant likelihood that an adversary or potential adversary in anticipated litigation will obtain it.

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## ***Other Protections of Confidentiality***

- 1. Confidentiality agreements**
- 2. Objections to discovery coupled with seeking protective order under Rule 26(c)(1)(A) (“forbidding the disclosure or discovery”)**
- 3. Return of documents to client after review by financing entity**
- 4. Maintenance of documents off shore**

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## ***Fee Splitting with Nonlawyers***

- Generally, a lawyer may not divide or share fees with a nonlawyer. See ABA Model rule 5.4(a)
- Not a problem in transactions involving purchase of portion of cause of action from client or loan to client because all payments come from client not lawyer
- Not a problem in cocounsel arrangements because fees are divided with other lawyers
- Fee splitting is only a potential problem in transactions involving loans to lawyers

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## ***Fee Splitting with Nonlawyers***

- Law firm payments of interest to the financing entity will come from legal fees earned by the firm, but the source of payment of cannot be the test for whether a payment involves fee splitting.
- If it were, it would prohibit firms from making ordinary business payments, such as salaries to nonlawyer employees, rent to landlords, or utilities to providers of such services.
- A number of ethics opinions have held that law firms may borrow money from financial institutions and repay the loan out of the firm's revenues. See also Douglas R. Richmond, *Other People's Money: The Ethics of Litigation Funding*, 56 Mercer L. Rev. 649, 676-681 (2005) (analyzing and rejecting arguments that litigation financing involves fee splitting with nonlawyers).

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### ***Fee Splitting with Nonlawyers***

- Since the source of a payment to a nonlawyer is not determinative as to whether the payment involves improper fee splitting, it is necessary to determine whether a particular fee payment to a nonlawyer violates the policies on which the prohibitions against fee splitting with nonlawyers are based.
- Comment 1 to Rule 5.4 states the following policy: “The provisions of this Rule express traditional limitations on sharing fees. These limitations are to protect the lawyer’s professional independence of judgment.” (emphasis added).

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### ***Fee Splitting with Nonlawyers***

Comment b to Restatement §10 expresses the same policy analysis of the prohibition against fee splitting but goes further:

- “The Section should be construed so as to prevent nonlawyer control over lawyers’ services, not to implement other goals such as preventing new and useful ways of providing legal services or making sure that nonlawyers do not profit indirectly from legal services in circumstances and under arrangements presenting no significant risk of harm to clients or third persons.” (emphasis added).

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### ***Independent Professional Judgment***

- To protect independent professional judgment of attorney, financing agreement should provide that lawyer and client retain right to make all decisions regarding the case, including the decision whether to settle.
- Analogous to insurance defense practice, although this financing relationship is less intrusive because insurance companies typically have the right to decide whether to settle (except in professional negligence cases).

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### ***Public Policy and Litigation Finance***

- Under current structure of litigation finance all of risk in litigation is born by client and lawyer. Exact allocation depends on agreement between lawyer and client.
- Neither lawyers nor ordinary clients (insurance companies excluded) are in the business of dealing with risk.

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### ***Advantages of Allowing Third Party Financing:***

- **Expanding Choice**
  - Allowing third party financing enables lawyers and their clients to shift risks to professional risk bearers in an amount that suits their needs and interests
- **Equality and Fairness**
  - Third party financing promotes equality and fairness in litigation by providing resources to financially weak parties
- **Efficiency**
  - Third party financing promotes judicial efficiency because settlements are more likely when both parties know that the other has the resources to take the case to trial if necessary

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### ***Example of Risk Allocation Effects of Third Party Financing***

- **Risk in litigation under current system**
  - Assume a case with a potential recovery of \$9 Million
  - Assume estimated expenses of \$200,000
  - Assume anticipated lawyer time valued at \$500,000
  - Assume probability of success of 50%
  - Assume firm advances all expenses
  - Assume contingency fee of 1/3 payable before expenses are deducted
- **Risk in litigation under current system**
  - If case is successful, firm receives \$3.2 million in fees plus expenses - \$200,000 in expenses paid - \$500,00 in lawyer time = \$2.5 million
    - Worst case = loss of (\$700,000)
    - All of risk on law firm

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### ***Example of Risk Allocation Effects of Third Party Financing (continued)***

- Transferring part of risk to client
  - Part of risk can be transferred. If client pays all litigation expenses, then firm's return if case is successful is \$3 million - \$500,000 in lawyer time = \$2.5 million
  - Worst case is -\$500,000 in lawyer time.
  - Commercial clients may be able and perhaps willing to pay expenses, but few individual clients can do so.

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### ***Example of Risk Allocation Effects of Third Party Financing (continued)***

- Transferring all of risk to third party provider of capital
  - Assume third party willing and able to absorb all of risk
  - Financier will pay all expenses and lawyer time in exchange for 60% of recovery after it recovers all its expenses. Remainder goes 1/3 to firm and 2/3 to client
  - Returns if case is successful are as follows:
    - \$9 million recovery. \$700,000 to financier to repay expenses and legal fees. 60% of balance to financier = \$4.98 million. Balance of recovery \$3.32 million. 67% to client = \$2.22 million. 33% to law firm = \$1.10 million
    - If case is settled for 50% of value, firm gets \$550,000 plus payment of all of its legal fees. Firm has no risk for expenses or legal fees

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*Bigelow v. Old Dominion Copper Mining & Smelting Co.*, 71 A. 153, 167 (N.J. Ch. 1908) (finding that the English statutes of champerty and maintenance had not been adopted by the state of New Jersey).

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## ADDITIONAL ARTICLES FOR REFERENCE

### **Refinancing Civil Litigation**

Stephen C. Yeazell

University of California, Los Angeles - School of Law

DePaul Law Review, Vol. 51, p. 183, 2001

#### **Abstract:**

This article argues that most of the important phenomena of modern litigation are best understood as results of changes in the financing and capitalization of the bar. During the twentieth century civil litigation has moved its focus from trial to discovery and settlement. Two elements coalesced to transform litigation practice: changed discovery rules and the spread of liability insurance. Much of that transformation involved changes in financial arrangements, both among defendants, with the spread of liability insurance, and among lawyers, with growth in firm size, and better diversification and capitalization of the plaintiffs' bar, and regulatory changes that enabled better marketing of firms' services. This reconfiguration was both necessary – because modern discovery required substantial investment – and profitable – because good discovery yielded improved settlements. As a consequence of these changes, lawyers at the end of the twentieth century offered clients improved, though more expensive, litigation services in a more competitive market with resources more evenly balanced between plaintiffs and defendants than at the start of the century.

#### **Accepted Paper Series**

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#### **Suggested Citation**

Yeazell, Stephen C., Refinancing Civil Litigation. DePaul Law Review, Vol. 51, p. 183, 2001.

### **Brown, The Civil Rights Movement, and the Silent Litigation Revolution**

Stephen C. Yeazell

University of California, Los Angeles - School of Law

Vanderbilt Law Review, 2004

#### **Abstract:**

Brown v. Board of Education had two collateral effects on the legal profession. First, it created a new set of professional heroes - plaintiffs' lawyers pursuing social reform through litigation. Second, it began the gradual deregulation of the bar, particularly the plaintiffs' bar. Both changes reached well beyond the original civil rights arena and both continue to shape the legal profession and the economics of civil litigation.

Keywords: Brown, plaintiffs' bar, deregulation, legal ethics

JEL Classifications: K22, K41

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#### **Suggested Citation**

Yeazell, Stephen C., Brown, The Civil Rights Movement, and the Silent Litigation Revolution. Vanderbilt Law Review, 2004.

## **Fee Regimes and the Cost of Civil Justice**

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Civil Justice Quarterly, Vol. 28, Issue 3, p. 344 (forthcoming June 2009)

### **Abstract:**

The issue of costs in civil justice processes is an enduring issue. Reforms are proposed, implemented, usually found wanting. Many of these reforms involve manipulating how lawyers are paid for their work in civil justice, a sensible approach given that lawyers' fees comprise a very large proportion of the costs of civil justice processes. All fee systems create a mix of positive and perverse incentives. Proposals to modify fee arrangements, either coming from reformers or from individual clients, typically fail to grasp the complexity of fee systems and how those systems interact with other aspects of the justice system. In this paper, I employ the construct of "fee regimes" to explicate these complications. Fee regimes as used here are comprised of three components: how fees are computed; who pays the fee; and how fees are regulated and/or reviewed. Every system involves all three elements in one way or another, and the interaction of the three elements makes it difficult to anticipate how modifying only one element will impact the incentives that motivate both lawyers and parties. Moreover, fee regimes are embedded into the expectations of the actors in a civil justice system, and those expectations are often unstated because they are assumed to be natural rather than endogenous to the fee regime. I conclude with a brief discussion of how those considering reforms might better try to anticipate the likely impacts of the changes they would make.