Justice Dealers: The Ecosystem of American Litigation Finance
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Stanford Journal of Law, Business & Finance; Fall 2015; 21, 1; ProQuest Central
pg. 98

Justice Dealers: The Ecosystem of American Litigation Finance

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Abstract. People litigate for various reasons. Some want to right wrongs, others—create precedents. But most, at least in the civil realm, sue to protect economic interests, and they are motivated by pragmatic considerations rather than abstract notions of justice. One fruit of the mercantile approach to civil litigation is the nascent market where third parties provide financing for litigants (or their lawyers) and profit from a successful resolution of the funded claims. Through the lens of a third-party funder, justice is a mass-market commodity, and its value depends on laws of men and laws of probability alike.

The ways of litigation funders create multiple points of tension for the legal process and its participants, and laws on the book offer little guidance on how third-party interests should be treated. Resulting procedural and ethical dilemmas have stirred a debate among scholars who rushed to offer conflicting opinions and advice. Critics demand that litigation investing be banned, calling it a travesty of justice that turns courts into casinos. Enthusiasts want the practice formally recognized, asserting that it levels the playing field for weaker parties.

The discussion on litigation financing does not lack vigor, but it does lack hard facts. Drawing from first-hand empirical data on the practice of litigation funding in the United States, this paper describes how the market for legal claims actually works. First, I sketch out the entire ecosystem of actors who apply the logic of asset management to uncertainties of individual lawsuits—litigants, litigators, funding companies and their investors, and their "entourage" providing additional, specialized services. Then I segment the market and explore different strategies of third-party investing. Finally, I list American litigation funders and group them based on what they do.

Based on the descriptive findings, I claim that modern civil litigation engages multiple, often undisclosed stakeholders with complex financial motivations. I argue that such interests should be recognized by the legal system as legitimate and ultimately regulated. The first step in that direction should be making sure that third-party involvement in a dispute is disclosed.

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I. The Elephant in the Room

The idea of litigation finance has been intriguing legal scholars in recent years, yet much confusion remains about what the practice consists of and how it works. In fact, the current state of academic research in that area brings to mind the moral tale about blind men and an elephant. In the story, different members of a group of blind men sought to learn what the creature looked like by touching it. Since each man touched but one part of the elephant, they each returned with very different answers to their "research question." Not only were the answers hard to reconcile, but they did not say much about the elephant as a whole.[1]

Luckily for the fabled research subject, the Indian blind men were not legal scholars. Had they been, they would have swiftly and assuredly rushed to offer advice on how to best police a trunk, a tusk, or a belly. Alas, litigation funding is a creature of law and finance, and so it has been pursued with the mind to offer policy advice first and to ask questions later.

Various scholars argue over whether legal funding levels the playing field for litigants or whether it merely encourages frivolous suits.[2] Some ethical questions relevant to funding arrangements with third parties have been thoroughly discussed in academic literature.[3] Litigation funding has also been compared across different legal systems.[4] An empirical foundation for these debates remains weak, however.[5]

1. I am grateful to Deborah Hensler for reminding me of this useful parable.

2. *See, e.g.*, Ronen Avraham & Abraham L. Wickelgren, *Third Party Litigation Funding—A Signaling Model*, 63 DEPAUL L. REV. 233 (2014); Elizabeth Chamblee Burch, *Financiers as Monitors in Aggregate Litigation*, 87 N.Y.U. L. REV. 1273 (2013); Susan Lorde Martin, *The Litigation Financing Industry: The Wild West of Finance Should Be Tamed Not Outlawed*, 10 FORDHAM J. CORP. & FIN. L. 55 (2004); Jonathan T. Molot, *Litigation Finance: A Market Solution to a Procedural Problem*, 99 GEO. L.J. 65 (2010) (all arguing in favor of litigation financing). *But see* Julia H. McLaughlin, *Litigation Funding: Charting a Legal and Ethical Course*, 31 VT. L. REV. 615 (2007); Paul H. Rubin, *Third-Party Financing of Litigation*, 38 N. KY. L. REV. 673 (2011) (arguing against); U.S. Chamber Inst. for Legal Reform, Selling Lawsuits, Buying Trouble: Third-Party Litigation Funding in the United States (2009), http://www.instituteforlegalreform.com/uploads/sites/1/thirdpartylitigationfinancing.pdf.

3. *See, e.g.*, Sheri P. Adler, *Alternative Litigation Finance and the Usury Challenge: A Multi-Factor Approach*, 34 CARDOZO L. REV. 329 (2012); Nora Freeman Engstrom, *Lawyer Lending: Costs and Consequences*, 63 DEPAUL L. REV. 377 (2014); Jason Lyon, *Revolution in Progress: Third-Party Funding of American Litigation*, 58 UCLA L. REV. 571, (2011); Stuart L. Pardau, *Alternative Litigation Financing: Perils and Opportunities*, 12 U.C. DAVIS BUS. L.J. 65 (2011); Douglas R. Richmond, *Other People's Money: The Ethics of Litigation Funding*, 56 MERCER L. REV. 649 (2004); Anthony J. Sebok, *The Inauthentic Claim*, 64 VAND. L. REV. 61 (2011).

4. *See, e.g.*, Jasminka Kalajdzic, Peter Cashman & Alana Longmoore, *Justice for Profit: A Comparative Analysis of Australian, Canadian and U.S. Third Party Litigation Funding*, 61 AM. J. COMP. L. 93 (2013); Marco de Morpurgo, *A Comparative Legal and Economic Approach to Third-Party Litigation Funding*, 19 CARDOZO J. INT'L & COMP. L. 343 (2011).

5. Few publications I am aware of rely on any empirical materials other than newspaper articles or Internet posts. Exceptions are: STEVEN GARBER, RAND, ALTERNATIVE LITIGATION FINANCING IN THE UNITED STATES: ISSUES, KNOWNS, AND UNKNOWNS (2010), http://www.rand.org/pubs/occasional_papers/OP306.html (overviewing the litigation funding market based on seventeen semi-structured, mostly phone, interviews); Engstrom, *supra* note 3 (referencing several phone interviews); and Maya Steinitz, *Whose Claim Is This Anyway?:*

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Moreover, the room for useful conversation is limited: despite the growing body of literature, academics have failed to establish a commonly accepted conceptual framework that would systematize the practice of financing lawsuits, litigants, and litigators.[6] Different scholars really talk about different things, even when they use the same terms.[7]

Here, I anchor the concept of third-party litigation funding in its economic nature, which I understand as the acquisition of a chance to take some of the value contested by two or more parties who assert rights enforceable through the process of law. When I discuss "third-party litigation funding" (or its variations), I use it as a term of art derived from practice, an imprecise shorthand covering various ways of buying into somebody else's interest in what is, was, or might be a lawsuit.[8] What I

Third-Party Litigation Funding, 95 MINN. L. REV. 1268 (2011) (using twelve anonymous background interviews with litigation funding insiders). There are also publications written by insiders of the funding industry. *See, e.g.*, Jonathan T. Molot, *The Feasibility of Litigation Markets*, 89, IND. L.J. 171 (2014). The latter—as well as scholars with deep ties to specific funding companies for which they repeatedly consult—undoubtedly benefit from the access to private empirical data and practical insights available to the authors. However, the same publications suffer from limited research validity, with the insider-cum-scholar (or the other way around) constrained by contractual obligations or fiduciary duties owed to a third-party financier. Consequently, a significant risk exists that the author may cross the line between legal scholarship and financially motivated advocacy. A good illustration of such potential is provided by the acerbic exchange between Professors Lester Brickman and Herbert Kritzer on the topic of contingency fees. *See* Herbert M. Kritzer, *Advocacy and Rhetoric vs. Scholarship and Evidence in the Debate over Contingency Fees: A Reply to Professor Brickman*, 82 WASH. U. L. REV. 477, 478 (2004) (criticizing his adversary for letting "his advocacy distort his scholarship" and for "a lack of training about the norms and practices of social science").

6. *See, e.g.*, Michele DeStefano, *Nonlawyers Influence Lawyers: Too Many Cooks in the Kitchen or Stone Soup*, 80 FORDHAM L. REV. 2791, 2796 (2011-2012) (arguing that third-party funding nomenclature is "all over the map and woefully undescriptive"); Engstrom, *supra* note 3, at 582-83 (observing that insufficiently nuanced analysis of different litigation funding models is their "glaring limitation"); Garber, *supra* note 5, at 9 (noting that different segments of the litigation funding market raise different concerns and must be considered separately); Steinitz, *supra* note 5, at 1302 (pointing out that debates about litigation funding tend to treat it "en masse, as if there is only one type of funding").

7. For illustrations of how widely scholars' definitions of litigation funding vary. *See*, *e.g.*, Kalajdzic, *supra* note 4, at 94 ("commercial financing of an individual or portfolio of lawsuits by a person or entity that is not a party to the litigation itself"); Lyon, *supra* note 3, at 573-74 (a combination of two "lending schemes": pre-settlement lawsuit loans to personal injury plaintiffs and "syndicated lawsuits" where a plaintiff sells shares of recovery to investors); Susan Lorde Martin, *Litigation Financing: Another Subprime Industry That Has a Place in the United States Market*, 53 VILL. L. REV. 83, 84, 87 (2008) (funding "poor individual plaintiffs" or "offering financing to lawyers to pursue lawsuits"); Pardau, *supra* note 3, at 66 (an agreement between a litigant and an "unrelated party" that buys a portion of proceeds); Richmond, *supra* note 3, at 650 (loans to plaintiffs or attorneys); Avraham & Wickelgren, *supra* note 2, at 237-39 (two types of loans: "debt-based" to individual plaintiffs and "equity-based" investments targeting cash-strapped, small companies).

8. Garber, *supra* note 5, at 1, coined the term "alternative litigation funding," or "ALF," defining it as "litigation financing . . . by entities other than plaintiffs, defendants, their lawyers, and defendants' insurers." This definition is problematic. First, it does not explain what "litigation funding" means. Second, it focuses on the financier, rather than the financing itself. Third, it assumes that "alternative" financing is really an alternative to contingency fees, which is not true. *See infra* Parts III.0IV.AFor a differently motivated critique of the litigation funding

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actually mean is a professional, systematic activity consisting of the provision of resources to stakeholders in legal disputes—holders of legal claims, causes of action, or underlying assets, as well as parties against whom such claims, actions, or asset rights are directed—by nonstakeholders in exchange for a pecuniary interest in the outcomes of funded disputes or another form of valuable consideration dependent on such outcomes.[9]

This paper offers a descriptive introduction to, and conceptual framework for, the American practice of litigation funding, providing an empirical springboard for further normative analysis and regulatory discussion. Part II sketches the regulatory environment of the American funding practice. Three subsequent parts focus on the surface anatomy of the "litigation funding elephant." Part III maps out main groups of actors with a stake in the funding practice. Part IV focuses on market segments and dominant investment strategies. And Part V identifies leading litigation funders operating in the United States and the main strategies they pursue.

II. Regulatory Framework

Litigation funding is like a river. How the river flows depends on the landscape it meets. The part of the litigation funding landscape presented in this Part is its regulatory framework, which influences how business gets done. However, just like a river finds ways around boulders and hostile ground, so, too, does the capital flowing from those who have it to where it is required. The resulting meandering may be a bit tricky to navigate, but the current will eventually carry the load from its source to the destination. This Part is about legal and ethical rules relevant for investing in disputes.

A. Control

A cardinal rule of business, one as old as trade and music, is that he who pays the piper calls the tune. Those who have capital expect a say on how it will be used—particularly when the goal is to make more money. That stating as much in the context of litigation finance should amount to a major criticism of the funding

nomenclature, see DeStefano, *supra* note 6, at 2796, 2833-40 (arguing that commercial funding is "not so alternative").

9. The suggested framing of the market for third-party financing of litigation leaves out those transaction where a third party champions a disputant's case for reasons other than profit. Specifically, I do not consider regulatory designs where prosecution of private rights is financed or otherwise supported by public agencies. This also excludes financial arrangements used by public-interest law firms and nongovernmental organizations to fund impact litigation. The non-profit funding of litigation is beyond the scope of this paper. Note, however, that for-profit funding (as understood here) and public-interest litigation are not mutually exclusive, as the former states the objective of the funder and the latter states the objective of the litigant and, often, her lawyer. In other words, under the right circumstances, it is entirely feasible that at least certain types of non-profit suits may be backed by a for-profit funder.

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practice,[10] and that those engaged in it would rush to renounce any ambition of calling the shots,[11] is quite telling.

Those focused on legal and ethical aspects of litigation finance tend to point to two major junctures at which control issues may arise: one is the litigant's right to select (and fire) a lawyer; the other is his authority to dispose of his claim.

As far as the attorney-client relationship is concerned, there is little doubt that the client's right to hire and fire a lawyer is almost absolute,[12] as is his power to settle his own case[13] and make other strategic decisions.[14] As between a client and a funder, however, it has been argued that there is no reason why the former could never contractually delegate those powers to the latter or promise to exercise them in a particular way.[15] Whether such a contractual arrangement would impermissibly interfere with the independent professional judgment of the attorney, obligating her to withdraw, is a question that remains to be settled.[16]

When a third party transacts with a lawyer, rather than her client, ethical concerns are even more pronounced. There, any degree of the funder's control of how the lawyer manages a case—or her entire practice—apart from the clear potential for conflicts of interest,[17] runs afoul of the rule which prohibits lawyers to practice law in a partnership where a non-lawyer holds a (nonfiduciary) interest, acts

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10. *See, e.g.*, Beisner, *supra* note 2, at 7 (claiming that funders "inherently desire to protect their investment and . . . to exert control over strategic decisions in the lawsuit").

11. *See, e.g.*, COMM. ON ETHICS 20/20, AM. BAR ASS'N, INFORMATIONAL REPORT TO THE HOUSE OF DELEGATES 26 (2012), http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111212_ethics_20_20_alf_white_paper_final_hod_informational_report.authcheckdam.pdf [hereinafter ABA WHITE PAPER] (stating that the working group "reviewed numerous contracts submitted by [litigation funders] that expressly disclaim any control by the [funder] over the settlement decision"). Statements by interviewed funder-side insiders support that sentiment: funders usually present themselves as "passive investors"; some do acknowledge a role in litigation decision-making, but merely in advisory capacity.

12. *See* MODEL RULES OF PROF'L CONDUCT r. 1.16(a)(3) (AM. BAR ASS'N 2011); *id.* r. 1.16 cmt. 4; RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 32(1) (AM. LAW INST. 2000); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 32(1) cmt. b; *see also* AFLAC, Inc. v. Williams, 444 S.E.2d 314 (Ga. 1994) (declaring a contractual penalty for terminating a retainer agreement by a client unenforceable); Reid v. Lansberry, 629 N.E.2d 431 (Ohio 1994) (holding that a client has an absolute right to discharge an attorney at any time, with or without cause, and that financial arrangements penalizing such a discharge are unenforceable); *In re* Wallace, 574 So. 2d 348 (La. 1991) (striking down a statute limiting executor's power to discharge attorney designated in testator's will to "just cause").

13. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 22(1), (3), cmts. b-d.

14. Those events include the decision whether to appeal or otherwise dispose of the action in a way that forecloses client rights. *See id.* cmts. d-e.

15. *See* WHITE PAPER, *supra* note 11, at 21, 27.

16. *Id.* at 27 (referring to MODEL RULES OF PROF'L CONDUCT r. 1.2(c), 1.16(a)(1)).

17. For example, the Michigan Bar examined an agreement where an attorney would refer her clients to a particular funder. Under that framework, the lawyer and each funded client were required to grant the funder access to all records, and delegate to him broad powers over litigation decisions, including selection of counsel. The setup was deemed unethical due to an irreconcilable conflict of interest it would create. *See* Mich. ST. B. Standing Comm. on Prof'l Ethics, Advisory Op. RI-321 (2000).

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in a managerial capacity, or is in a position to otherwise direct or control the professional judgment of a lawyer.[18] Any control or direction by a third party, even when it pays the lawyer's fees, is permitted only insofar as it pertains to a representation of a particular client who transferred his authority to instruct the lawyer to that third party.[19]

In practice, many third-party financiers obtain a degree of *de facto* control over their investments, often without explicit contractual authority. A funder's influence may reflect his power to cut off the money before the case is resolved, his repeated dealings with a particular law firm and tacit expectations that such dealings create, or the possibility that the funder may sway clients to seek another representation.

B. Conflicts of Interest

A third-party funding arrangement involves at least three parties: the claimholder, the attorney, and the funder. In such a relationship, there exists an obvious potential for a conflict of interest, one which the complexity of the arrangement and the number of parties involved may only exacerbate.

As a rule, lawyers are prohibited from representing clients in the presence of a "concurrent conflict of interest," which encompasses a situation where the lawyer is at risk of being materially limited in his representation by personal interests or responsibilities to a third party.[20] However, the affected client may waive the conflict if he gives a written, informed consent.[21] Likewise, unless the terms are fair, and the well-informed client agrees in writing, a lawyer must not acquire a pecuniary interest adverse to that of an existing client[22] or use information relating to her representation against the client.[23]

In the context of litigation funding, a lawyer may likely find herself in a conflict of interest any time she wears two hats at the same time—for example, when she represents both the client and the funder or when the funder pays the lawyer a fee for referring the client-cum-fundee.[24]

In some situations, the question of divided loyalties does not arise—for instance, a lawyer does not put herself into trouble when she pays the funder from proceeds of a lawsuit as promised by the client under a valid contract.[25] But sometimes, the lawyer treads a much finer line. For one, an attorney may have a long-term working

18. *See* MODEL RULES OF PROF'L CONDUCT r. 5.4(b)-(d).

19. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 134(1), (2), cmt. d.

20. *See* MODEL RULES OF PROF'L CONDUCT r. 1.7(a).

21. *See id.* r. 1.0(e), 1.7(b). The waver is an option if the representation is legal. And a lawyer may never represent clients with adverse interests in the same case. *See id.*

22. *See id.* r. 1.0(e), 1.8(a).

23. *See id.* r. 1.8(b).

24. *See* ABA WHITE PAPER, *supra* note 11, at 17.

25. *See, e.g.*, Leon v. Martinez, 638 N.E.2d 511 (N.Y. 1994).

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relationship with a specific financier.[26] Should interests of the funder diverge from those of her client, the lawyer could find herself in a conflict.

There are multiple real-life scenarios suggesting that lawyers do not always behave as prescribed by the rules of legal ethics. In particular, third parties may finance both the client and his lawyer against their respective interests in a lawsuit. An attorney could be tempted to share information about a client and his circumstances—either to encourage a third-party investment (which would include paying the lawyer's bills), or to protect her relationship with a funder. It may be that a lawyer is funded by a financial institution which is an affiliate of the party which the lawyer, on behalf of a client or a whole class of clients, sues in court. Or she might hold contingency interests in a series of related cases, funding or strategically sharing some of them to improve the value of her stakes in other suits.

C. Fee-Sharing

In the United States, unlike in many other jurisdictions, it has since long been recognized that a lawyer may profit from a settlement or trial win in the form of "a reasonable contingent fee" negotiated with the client.[27] A contingency fee has been the default legal device used to transfer an equity stake in a legal dispute to a qualified third-party—a lawyer who, at least formally, has been appointed as counsel on the case in question.

On the other hand, with some narrow exceptions, rules of legal ethics prohibit lawyers from sharing fees (or profits from the practice of law) with non-lawyers—supposedly to protect the independent professional judgment of lawyers.[28] This rule has been the subject of an ongoing, and at times tempestuous, debate within the American Bar, but it has received little attention in the context of litigation funding.[29] This is a pity, as the issue of lawyers sharing proceeds from their cases is central to those models of third-party funding where money is injected into disputes indirectly through law firms.[30]

Co-investing with lawyers is a growing trend in business-to-business litigation funding. Yet lawyers cannot reward their capital partners with an "equity stake," either in a law firm as a going concern or in a limited portfolio of legal cases subject to alternative-fee arrangements. This results in various workarounds: dressing up an

26. *See* ABA WHITE PAPER, *supra* note 11, at 16-17.

27. *See* MODEL RULES OF PROF'L CONDUCT r. 1.8(i).

28. *See id.* r. 5.4.

29. For example, the ABA White Paper covers fee sharing in exactly two paragraphs, one of which states the rule. *See* ABA WHITE PAPER, *supra* note 11, at 29.

30. *See* Radek Goral, *The Law of Interest Versus the Interest of Law, or on Lending to Law Firms*, 29 GEO. J. LEGAL ETHICS (forthcoming 2016) (describing how third-party funders use sophisticated debt arrangements to invest in various types of law firms and the attorneys' fees such firms hope to earn) [hereinafter Goral, *The Law of Interest*]; Radek Goral, *A Matter of Trial and Error, Or Betting on Appeals*, 91 NOTRE DAME L. REV. ONLINE 50 (2015) (giving examples of appellate cases where a funder acquired a stake in the judgment interests of both the plaintiff and her attorney).

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"equity partner" in the robes of a creditor, or funneling money through special-purpose law firms.

D. Confidentiality and Privilege

When deciding whether to fund a case and how to price their risk, financiers need information; therefore, they are usually legitimately interested in private information the potential fundee may have. But once such private information is shared, it may no longer be private. Therefore, how the law protects confidential information related to a dispute matters for litigation funders, potential fundees, and their lawyers. Three legal theories are relevant here: the duty of confidentiality, the attorney-client privilege, and the work-product doctrine.[31]

The duty of confidentiality is the broadest of the three, as it obligates the lawyer not to disclose any "information relating to the representation of a client" without the client's informed consent.[32] At the same time, the duty only pertains to relationships between attorneys and their clients, and, in itself, offers no protection from discovery in litigation.[33]

The attorney-client privilege does afford protection against discovery by an adversary, but it is limited to communications made in confidence by "privileged persons" in connection with legal assistance provided to the client.[34] Each of the above prongs is subject to interpretation, rendering the scope of the privilege jurisdiction- and case-specific.[35] The information covered by the privilege is protected by the lawyer's duty of confidentiality, and she must act competently to preserve it—against third-party incursions or inadvertent disclosure.[36]

Sharing protected information with a non-privileged party would normally waive the privilege.[37] But if the client and the party to which the disclosure is made are deemed to have a "common interest," the privilege holds—even if they are represented by different attorneys.[38]

31. *See* MODEL RULES OF PROF'L CONDUCT r. 1.6, cmt. 13.

32. *See id.* r. 1.6(a).

33. *See* ABA WHITE PAPER, *supra* note 11, at 31.

34. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 68 (AM. LAW INST. 2000). "Privileged persons" include the attorney, the client, and agents of the lawyer who facilitate the representation. *See id.* § 70. Payment of legal fees is not, by itself, sufficient for the privilege to cover the payer who does not himself seek legal assistance. *See, e.g.*, Priest v. Hennessy, 409 N.E.2d 983 (N.Y. 1980).

35. *See* ABA WHITE PAPER, *supra* note 11, at 31 n. 120, 33.

36. *See* MODEL RULES, *supra* note 12, r. 1.6(c), cmts. 13, 15, 18-19.

37. *See* United States v. Bernard, 877 F.2d 1463, 1465 (10th Cir. 1989); PAUL D. RICE, ATTORNEY-CLIENT PRIVILEGE IN THE UNITED STATES § 9:28 (2d ed. 1999).

38. *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 76; RICE, *supra* note 37, § 4:35. Although most authorities agree that the interests between clients need not be identical, they must be "substantially similar" legal, as opposed to merely economic, interests. *See In re* Teleglobe Commc'n Corp., 493 F.3d 345, 365 (3d Cir. 2007); *see also* Miller UK Ltd. v. Caterpillar, Inc., 2014 WL 67340 (N.D. Ill. 2014); Leader Techs., Inc. v. Facebook Inc., 719 F. Supp. 2d 373, 376 (D. Del 2010). When parties discuss business matters, their communications may still be deemed privileged, as long as they are "infused with legal

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The third theory protecting confidential information of a litigant, which most jurisdictions have on the books as a rule of procedure, is the work-product doctrine.[39] It pertains to physical expressions of a litigation-related thought process—"documents and tangible things otherwise discoverable . . . . prepared in anticipation of litigation or for trial by or for another party or by or for that other party's representative."[40] The protection of the work-product doctrine is narrow, but hard to pierce. It may be deemed waived only when disclosure substantially increases the chance of making it accessible to a lawsuit opponent.[41]

Although some funders claim that they never seek privileged information, others look for creative ways to access it. For example, a funding agreement may provide that the fundee shall appoint an additional, "designated counsel," approved by the funder, and that the fundee shall instruct such counsel to keep the funder informed to the extent possible without triggering a waiver. Or the fundee may be required to appoint as co-counsel an officer of the funder who also happens to be a lawyer, effectively giving the funder a seat at the table. Some funders simply debrief the fundee and/or the lawyer in a private setting, without any "paper trail" of the matters discussed, realizing that a disclosure made is not the same as a disclosure proved by an adversary.

E. Duty to Disclose Funding

In the context of litigation finance, the duty of confidentiality finds its inverse in the duty to disclose funding. Such duty should be considered on two planes: internal, as between the client and the attorney; and external, made to the court and adversaries.

When a lawyer funds a represented case with third-party money, he may be under duty to disclose his financial arrangement with the third party to the client whenever it puts the lawyer's interests at odds with the client's. In such case, the duty to disclose stems from the rules of professional conduct governing conflicts of interests.[42]

In practice, under the existing rules of ethics and absent a direct relationship between the client and the financier, the lawyer has much discretion in deciding whether the attorney-funder link is problematic enough to merit disclosure. And since attorneys generally have little incentive to voluntarily share their financial position with clients, the latter may never know that their counsel "rehypothecated" his lawsuit stake.

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concerns." MobileMedia Ideas LLC v. Apple Inc., 890 F. Supp. 2d 508, 515 (D. Del. 2012) (quoting E. Pa. Transp. Auth. v. Caremarkpcs Health, L.P., 254 F.R.D. 253, 258 (E.D.Pa.2008)). It is dubious whether discussions with a third party except waiver of the privilege.

39. *See, e.g.*, FED. R. CIV. P. 26(b)(3).

40. *Id.*

41. *See, e.g.*, 8 CHARLES A. WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE § 2024 (1998).

42. *See supra* Part II.II.B

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External disclosure of funding to the court and adverse parties might also be relevant to avoiding conflicts of interest, as those disclosures are not limited to relationships between same-side actors. Moreover, such disclosures may be relevant for identifying real parties in interest and establishing liability for costs.[43] A party may also want to know if her opponent is funded for pragmatic reasons.[44]

Although an external disclosure of third-party funding transactions would serve several interests, there are few procedural tools compelling a spotlight-shy financier to make a court introduction. In particular, federal civil procedure in Rule 7.1 requires that a party to a lawsuit disclose its corporate parent and all its publicly held affiliates holding a stake of at least ten percent in the corporate litigant.[45] But the primary purpose of the rule is to help judges identify reasons for their financial disqualification, and its scope is intentionally narrow[46]— too narrow to, without more, effectively screen parties for third-party funding.[47] Even in those cases where a procedural basis for corporate disclosure does exist, it might be difficult to enforce.[48]

There is also no specific requirement that parties report third-party funding under Rule 26, even though insurance contracts under which an insurer may be liable to pay a judgment generally must be disclosed.[49] And while critics postulate that Rule 26

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43. *See infra* Part II.H.II.B

44. Knowing who stands behind a lawsuit matters for assessing the financial stamina of the opponent and her propensity to settle. And a disclosed presence of a third-party financier may make the judge or, if admissible, the jury, less sympathetic to the funded litigant and thus less willing to decide the case in his favor.

45. *See* FED. R. CIV. P. 7.1.

46. *See* FED. R. CIV. P. 7.1 advisory committee's note to 2009 amendment; *see also* Scheibler v. Highmark Blue Shield, 243 F. App'x 691, 694 (3d Cir. 2007).

47. Many district courts adopted local rules mandating more robust corporate disclosures. *See, e.g.*, N.D. CAL. CIV. L.R. 3-15(1)(b) (requiring parties to file a certificate disclosing any person known by the party to have a financial interest in the case or in a party to the proceeding, or any other kind of interest that could be substantially affected by the outcome of the proceeding).

48. Enforceability concerns were one of the explicit reasons behind the decision to draft Rule 7.1 narrowly. *See* FED. R. CIV. P. 7.1 advisory committee's note to 2009 amendment.

49. *See* FED. R. CIV. P. 26(a)(1)(iv). When introducing an amendment necessitating disclosure of insurance coverage, the Advisory Committee asserted that the rule would "enable counsel for both sides to make the same realistic appraisal of the case," pointing out that insurers often control litigation and that insurance is an asset tied specifically to a legal claim. *See* FED. R. CIV. P. 26 advisory committee's note to 1970 amendment.

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should be amended to require disclosure of third-party funding contracts,[50] their position implicitly concedes that there is no such requirement as a matter of existing law.

F. Usury

Usury is a practice of lending money at unreasonably high costs. Most states have set maximum interest rates which lenders may charge, subject to civil and even criminal penalties; however, broad categories of commercial debt transactions are typically exempt from statutory limits.[51] It follows that in the context of third-party funding, usury restrictions matter insofar as the funder-fundee relationship qualifies as a loan or similar debt transaction.

Unsurprisingly, many funders insist that what they provide is an advance, rather than a loan, because repayment by the fundee is contingent. Courts generally seem supportive of that argument.[52] Therefore, the issue is relevant mostly for law-firm financiers, since their business model consists of proper, full-recourse lending.

G. Champerty and Maintenance

"[M]aintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty."[53] In other words, champerty is for-profit maintenance. These medieval doctrines have their source in the fear that a litigant and her champion might abuse the legal process out of spite or for another wrong

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50. In a submission to the Committee on Rules of Practice and Procedure, the U.S. Chamber Institute for Legal Reform and several other business organizations proposed a mandatory disclosure of third-party financing in the form of an amendment to Federal Rule of Civil Procedure 26(a)(1)(A). *See* Letter from Lisa A. Rickard, President, U.S. Chamber Inst. for Legal Reform, et al. to Jonathan C. Rose, Sec'y, Comm. on Rules of Practice & Procedure of the Admin. Office of the U.S. Courts (Apr. 9, 2014), http://www.instituteforlegalreform.com/uploads/sites/1/4_-_final_version_-_tplf_disclosure_letter_4_9.pdf (last visited Dec. 5, 2014). The proposal elicited a stern rebuke from leading commercial funders—Gerchen Keller, Burford, and Bentham IMF—who in a letter to the Committee objected to mandatory disclosures. *See* Letter from Adam R. Gerchen, Chief Exec. Officer of Gerchen Keller Capital, LLC, at al. to Jonathan C. Rose, Sec'y. Comm. on Rules of Practice & Procedure of the Admin. Office of the U.S. Courts (Oct. 21, 2014), http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/cv-suggestions-2014/14-CV-B-1-suggestion.pdf (last visited Feb. 14, 2015).

51. In New York, the highest legally allowed interest rate is sixteen percent per annum. *See* N.Y. GEN. OBLIG. LAW § 5-501 (2015); N.Y. BANKING LAW § 14-a (2015). A rate exceeding twenty-five percent per annum is considered criminally usurious. *See* N.Y. PENAL LAW § 190.40 (2015). Most loans are exempt from civil usury when the principal is $250,000 or more, and from criminal usury when the principal is $2.5 million or more. *See* N.Y. GEN. OBLIG. LAW § 5-501(6).

52. *See, e.g.*, Dopp v. Yari, 927 F. Supp. 814 (D.N.J. 1996); Kraft v. Mason, 668 So. 2d 679 (Fla. Dist. Ct. App. 1996); Nyquist v. Nyquist, 841 P.2d 515 (Mont. 1992); Anglo-Dutch Petroleum Int'l, Inc. v. Haskell, 193 S.W.3d 87, 96 (Tex. Ct. App. 2006).

53. *In re* Primus, 436 U.S. 412, 425 (1978).

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reason.[54] Today, the risks underlying these doctrines are largely contained by the tort actions which the unduly harassed opponent has at her disposal.[55] The majority of American jurisdictions allow at least some forms of champerty as long as it does not promote "frivolous" litigation, is not motivated by "malice," and does not "intermeddle" with the normal course of the supported action.[56]

The main practical relevance of these antiquated doctrines for third-party funding of litigation lies in the legal and ethical uncertainty that they create for putative funders and fundees, given that in a number of states neither courts nor legislatures have spoken clearly on the subject.[57]

II. Liability for Costs

A practical question related to the maintenance issue is whether a third-party financier should be treated as a party in interest—which becomes particularly relevant when the fundee loses and the prevailing adversary moves for costs. The issue certainly deserves to be part of the public policy discussion on legal finance.[58] As a matter of existing law, however, it remains far from settled. While some courts have chosen to treat funders as parties liable for costs, the opposite conclusion appears to be more prevalent.[59]

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54. For history of maintenance, see Sebok, *supra* note 3, at 88-94.

55. *See, e.g.*, Sec. Underground Storage, Inc. v. Anderson, 347 F.2d 964, 969 (10th Cir. 1965) ("[T]he existing remedies [against maintenance] are through tort actions such as malicious prosecution, abuse of process, and wrongful initiation of litigation.").

56. *See* Sebok, *supra* note 3, at 98-99, 102, 104, 109.

57. Some states confirmed that they have never adopted the doctrine of champerty, or explicitly abolished it by case law or statute. Those include Arizona, California, Colorado, Connecticut, Florida, Massachusetts, New Jersey, New Hampshire, New Mexico, New York, South Carolina and Texas. Several jurisdictions, such as Minnesota or Alabama, seem to have reaffirmed the doctrine, although in a particular factual setting. For details, see ABA WHITE PAPER, *supra* note 11, at 11-12.

58. A recent decision by an English court in a high-profile case financed in substantial part by funders operating in the United States is an important precedent offering comparative insights. The case, Excalibur v. Gulf Keystone, [2013] EWHC 2767 (Comm) (Eng.), was a dispute over an alleged joint venture meant to exploit oil fields in Kurdistan. Excalibur, backed by a consortium of third-party funders and represented by Clifford Chance (who helped put the financing deal together), demanded about $1.75 billion in damages. *Id.* ¶ 6. After five months of trial, the plaintiffs suffered "a resounding, indeed catastrophic, defeat." Excalibur v. Gulf Keystone, [2013] EWHC 2767 (Comm) (Eng.), ¶ 9. The court berated Excalibur and Clifford Chance for what it believed was "in some circumstances highly aggressive and in others unacceptable" tactics, *id.* ¶ 48, and criticized a key executive and principal witness for the plaintiff as "a man long on assertion and confidence, but short on analysis and understanding [who] pursued this litigation as if it was an act of war," *id.* ¶ 12. Although Excalibur paid about £17.5 million as a security for costs, presumably with the third-party money, it was ordered to provide additional £5.6 million. *Id.* ¶¶ 68-76. The order specified that should the plaintiff fail to do so, the defendants would be allowed to seek costs from the third-party funders. *See id.* ¶¶ 80-86.

59. *See* Miller UK Ltd. v. Caterpillar, Inc., 67340 17 F. Supp. 3d 711 (N.D. Ill. 2014) (funder paying litigation expenses but holding no legal interest in the case is not liable for costs); Miccosukee Tribe of Indians v. Bermudez, 145 So. 3d 157 (Fla. Dist. Ct. App. 2014) (a funder entitled to part of recovery and influencing key lawsuit decisions may be a real party in

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III. Stakeholders Mapped Out

Third-party financing of legal claims is often seen as a transaction among three actors: the person who has an economically valuable claim (the claimholder), the person willing to bet money on that claim (the funder), and and the person getting paid to see the case through (the lawyer). Who those three actors are, and how they relate, is central to the business of litigation funding, and this paper explores both of those questions in detail. But although the litigant-attorney-funder trio is at the heart of every funding arrangement, the ecosystem of litigation finance includes others, too (although the others do not necessarily feature in every transaction). The purpose of this Part is to identify main types of actors operating in the American market for litigation funding and outline their respective roles.[60]

A. Fundees

It is tempting to state that in terms of litigation roles, the person who receives the money is the plaintiff to a lawsuit. But that is not exactly how things work. While much of litigation finance activity is indeed focused on the plaintiff side, defendants may also be funded through litigation finance. This category includes insurance: both before-the-event (where the insurer, in exchange for a premium, promises to indemnify the insured party against certain types of legal claims) and after-the-event (where the risk of liability is transferred after a legal dispute has already arisen). In the United States, insurance against litigation is usually bundled with protection against other risks and is offered as before-the-event insurance. The after-the-event model, viable on both sides of the bar, is popular in other jurisdictions.[61]

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interest liable for attorney's fees, as long as lawsuit was vexatious or wrongful); Abu-Ghazaleh v. Chaul, 36 So. 3d 691, 694 (Fla. Dist. Ct. App. 2009).

60. Since this paper is meant to provide a systematic description of the litigation market, the focus here is on direct stakeholders in dispute investments. However, there are at least two groups of actors other than those explicitly distinguished in this section whose role for the litigation funding market is profound, if indirect. Judges are one such group, and their ability to take stock of various funding arrangements, as well as their attitude towards funding in general, will be of increasing importance for the funded litigation and tactical decisions made by parties. *Cf.* Radek Goral, *The Color of Money: A Story of One Complex Case and its Many Financiers*, 12 N.Y.U. J.L. & BUS. (SPECIAL ISSUE) (forthcoming 2016) (manuscript at 21-24) (studying the interplay between funding arrangements and procedural decisions in the context of complex litigation).

    Insurers make another category of actors important for litigation funding, *see infra* note 61 and accompanying text. Indeed, the relationship between the idea of litigation funding and insurance has been noticed and vigorously debated in the literature. *See* Jonathan T. Molot, *A Market in Litigation Risk*, 76 U. CHI. L. REV. 367, 376-77 (2009); Anthony J. Sebok, *Betting on Tort Suits After the Event: From Champerty to Insurance*, 60 DEPAUL L. REV. 453 (2011); Steinitz, *supra* note 5, at 1295-96, 1310-12, 1334-46 (all arguing in favor of the analogy between litigation funding and insurance). *But see* Michelle Boardman, *Insurers Defend and Third Parties Fund: A Comparison of Litigation Participation*, 8 J.L. ECON. & POL'Y 673 (2012); Catherine M. Sharkey, *The Vicissitudes of Tort: A Response to Professors Rabin, Sebok & Zipursky*, 60 DEPAUL L. REV. 695 (2011) (both arguing the opposite).

61. For instance, in Greenclean Waste Mgmt. Ltd. v. Leahy [2013] IEHC 74 (H. Ct.) (Ir.), the High Court of Ireland defined the after-the-event insurance as "a form of insurance taken out in the wake of the specific event . . . . The premium is generally high, but is only payable

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Another kind of defendant-side funding involves a "defendant's contingency." There, the funder promises to cover some or all of the cost of defense; in exchange, the defendant promises to pay the funder an amount related to what she will have "saved" in the dispute—provided that an agreed litigation objective (such as having the case dismissed) is achieved.[62]

There are several reasons why such a model of funding is not very attractive to American defendants, particularly corporations. First, many of them can afford to "defend vigorously" against a suit with their own money. Second, a "defendant's contingency" requires that the defendant and the funder agree that the former is liable, and how much such liability is reasonably worth. In practice, those conditions are not easily met.

To summarize: a fundee does not have to act as plaintiff; it is possible, if not easy, to also fund a defendant. But a fundee does not even need to be a litigant. The importance of this last observation cannot be overstated, for much of the funding practice in American litigation is indirect, with third-party money injected into lawsuits through someone other than a disputant. That someone else usually turns out to be a party's attorney.

Depending on a particular configuration and relative bargaining power of the parties, the role of the litigant whose case is funded (but who does not necessarily act as the fundee) varies considerably. He may be a major stakeholder, hiring third-party capital for his own devices. But he may also be little more than a procedurally convenient nominee for third-party interests. In economic terms, the litigant then becomes a supplier of an investible claim and legal standing.

B. Funders

The role of a funder is predominantly that of an asset manager—he invests other people's capital. A funder's job is to pick fundable stakes in disputes for value and make sure they live up to their potential. To that end, a funder first has to "source" investments, or find prospective fundees. Second, a funder "underwrites" candidate cases: he assesses their quality and tries to price them. Then he selects claims which not only offer good value for the money, but also match his strategy and portfolio structure. Third, he acquires selected stakes, bargaining over the balance of rights and obligations of himself, the fundee, and possibly also other parties. Once a funding

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following successful costs recovery against another party." In a related ruling, the court acknowledged that this insurance may be "simply a disguised method of investing in litigation and recovering a share of the proceeds of the action under the guise of a handsome premium," Greenclean Waste Mgmt. Ltd v. Leahy (No 2) [2014] IEHC 314 (H. Ct.) (Ir.), ¶ 26. In England, effective April 2013, Section 58C of the Courts and Legal Services Act 1990 explicitly recognizes that a party may take out "costs insurance policy," defined as "a policy insuring against the risk of the party incurring a liability in [the] proceedings."

62. For example, if the defendant believes her exposure to a lawsuit is $100 million, she could agree to pay the funder, who would defend the lawsuit at his own expense, twenty-five percent of the difference between such expected liability and the actual outcome in the case. So that if, for instance, the case ended with the jury awarding the plaintiff $60 million, the defendant would "win" $40 million, and she would pay the funder $10 million out of the money "saved."

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transaction closes, the funder continues to manage the investment: he monitors the case, and sometimes also partakes in its development.

The sourcing-underwriting-contracting-monitoring structure of an investment cycle is quite general (managers investing in other kinds of assets follow a similar process). But what each of the stages looks like, and whether a financier subscribes to a "hands-on" or "hands-off" policy depends on the model of financing and preferred management philosophy.

As far as management is concerned, litigation funders attract mainly people with backgrounds in law or, to a lesser extent, finance. What may be of surprise, though, is that lawyers-cum-fund managers who deal mainly with plaintiff-side litigation seem to be dominated by corporate lawyers or former defendant-side litigators.

The explanation of this phenomenon lies in the managerial role of a funder, who acts as an intermediary between investors interested in "legal risks" and direct litigation stakeholders. Quite simply, funders rely on their relationships to find both money and cases. Corporate lawyers on a funder's roster are valuable because, among other things, their personal networks allow them to relate to the "right" people.

The financing-within-own-network story extends not just to those who presently manage companies providing legal funding, but also to those who are very conspicuously absent: power figures of the plaintiff bar. Some of them are themselves incumbent third-party financiers of litigation. They act as "banker lawyers," using proceeds from victories past to bankroll new cases in which their co-counsel do most (if not all) of the legal work. Other heavyweights of the plaintiff bar choose to stay away because they have access to external working capital with better terms. They are served by another class of incumbent financiers—commercial banks with whom plaintiff-side firms have long-term relationships.[63]

It is important to note here that dedicated funds investing in legal disputes are not the only game in town. Strictly speaking, lawyers and traditional commercial banks should also be counted as third parties providing capital used to finance prosecution of legal disputes.

C. Investors

Identifying whose money bankrolls American suits is a key piece of the litigation finance puzzle. Yet no researcher has as much as asked that question, much less answered it, with many assuming that funders and investors are more or less the same thing. As explained in the previous section, they usually are not. Third-party funders are middlemen responsible for mobilizing investment capital and deploying it to identified targets. Put differently, litigation is bankrolled with investors' money; but it is the job of a funder to put that money to work—by picking appropriate cases and ensuring that the capital is ultimately returned to its owners with a profit.

63. Goral, *supra* note 60 (manuscript at 7-16) (studying relationships between counsel to a large class action and various banks, and finding a pattern of long-term dealings between the two).

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Taking a look at the source of money wielded by third-party funders might seem superfluous, since all financial institutions are in the business of handling somebody else's capital. But following the money usually reveals who stands to benefit. More importantly, though, there is a powerful relationship between the source of capital a funder is able to tap and what he is able to fund, and how.

Because money trickles down from investors to lawsuits, what happens with the owners of the investible capital impacts those who hope to get it. Liquidity crunch affecting a funder may strangle claims brought forth with the expectation that third-party money would sustain them.[64] Similarly, poor performance of "litigation assets" may cause backlash from investors and force the funder to either promptly find an alternative source of money, or go back on his funding commitments.[65]

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64. Take, for example, Stillwater Asset Backed Fund, LP. Founded in 2004, the Stillwater family of funds comprised three main classes of assets: subprime mortgages, loans to contingency law firms, and insurance premium financing. *See* Objection of Stillwater Asset Backed Offshore Fund Ltd. to Motion for Appointment of Chapter 11 Trustee, *In re* Stillwater Asset Backed Offshore Fund Ltd., 485 B.R. 498 (Bankr. S.D.N.Y. 2012), ECF No. 13 [hereinafter Stillwater Objection], ¶¶ 2-3. A large stake in the Stillwater Funds (about $30 million) were acquired by Eden Rock Finance, an English hedge fund. *See* Eden Rock Fin. Fund, L.P. v Gerova Fin. Group Ltd., 34 Misc. 3d 1205(A)(2011) (denying defendants' motion to dismiss). In March of 2008, Eden Rock decided to withdraw; but Stillwater had its money frozen in illiquid pools of loans, and due to the plunging real estate market it was unable to return all the money. *See* Stillwater Objection, *supra*, ¶¶ 5-6. Smelling trouble, others soon wanted out as well; Stillwater offered to pay in kind, by transferring to investors-cum-creditors pro-rated participations in its assets; but the transaction proved difficult to execute. *See id.* ¶¶ 7-12. Facing a choice between liquidation at fire-sale prices and a bailout, they chose the latter, in the form of a merger with Gerova Financial Group, Ltd. *See id.* ¶¶ 19-40. The deal turned out to be controversial, with many investors suspecting foul play, and resulted in three class actions, *see* Stipulation and Agreement of Settlement, In Re Gerova Fin. Group, Ltd., Sec. Litig., No. 11-md-2275 (Oct. 06, 2011), ECF No. 73, ¶¶ A, B, G, L, S (listing all civil and bankruptcy actions against Gerova and Stillwater). The global settlement reached by the parties gave Stillwater creditors about two cents on each dollar invested. *See* Reply Memorandum for Final Approval of Settlement, *In re:* Stillwater Capital Partners Inc. Litig., No. 11-cv-2737 (S.D.N.Y. Apr 21, 2011), ECF No. 152 [hereinafter Stillwater Plaintiff Memorandum], 4.

At the end of the day, Stillwater went out of business—because of the financial crisis and its bet on underwater mortgages. The "collateral damage" caused by the subprime lending meltdown was Oxbridge Financial Group, LLC, which managed the portfolio of "litigation assets" for Stillwater, and the clients who through no fault of their own were suddenly left without a source of working capital. Some of them sued, including Mark Tate, an attorney from Georgia specializing in mass tort and personal injury. In 2007, Oxbridge granted The Tate Law Group, LLC a three-year revolving credit of up to $7.5 million. In return, Mr. Tate promised to bank only with Oxbridge, pay financing fees, and abide by other covenants. *See* Tate Law Group v. Stillwater Funding, LLC, 2012 N.Y. Slip Op. 33505(U) (N.Y. Sup. Ct. 2011) (granting motion to dismiss), at 2-3. In 2010, Mr. Tate was informed that he could no longer draw under the line of credit. The lawyer then sued, claiming that as a result of the funder's default he had to terminate employees, cancel contracts, and "reject cases that would have otherwise been accepted, and either enter into co-counseling agreements or refer cases to other law firms." *See* Verified Complaint at 8, Tate Law Group v. Stillwater Funding, LLC, 2012 N.Y. Slip Op. 33505(U), ¶ 44-45.

65. Consider RD Legal Capital, LLC [hereinafter RDLC], a third-party funder focused on post-settlement financing for plaintiffs and their lawyers. According to its investment memorandum, RDLC would pay its investors the first 13.5 percent of net annual profits, and it could keep any excess return. *See* Complaint, RD Legal Offshore Fund, Ltd. v. Paragon

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Moreover, the source of capital is important for litigation funders and the cases they intend to fund because of potential conflicts of interest.[66] Funders are disinclined to bite the hand that feeds them and back suits against the very people on whom they rely for capital. Likewise, institutional investors are wary of investments likely to cause them trouble or embarrassment. American businesses, cautioned by critics of third-party funding about "investors [who] have high risk appetites and are willing to back claims of questionable merit,"[67] would rather not hear that those investors are in fact their own peers or, worse, members of their own corporate families.[68]

Comity, like most other things in finance, has its reservation price, however. Norms of financial etiquette are binding only insofar as they do not dictate the unconscionable—that one abandons a profitable opportunity for nothing. Big-league money still finds its way to alternative "legal assets" (direct or indirect economic stakes in legal claims); but it often also chooses alternative routes considered to be more safe. Such routes include funneling money through intermediaries or taking property interests in entities that stand to benefit financially from a successful resolution of a legal dispute, notably attorneys and law firms.

In the United States, funders have been raising money for litigation ventures in three main ways. They organize "Evergreen funds" equipped with permanent capital, form private funds resembling private-equity partnerships, or leverage with debt.

The first option—raising money locked up in a permanent fund—is generally only available for the "whales" able to impress large investors. For example, two litigation funds, Burford and Juridica, raised about $500 million between them through the capital market—they are both listed on London's Alternative Investment

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Outcomes Fund I Class B, GML Ltd., No. 650246/2013 (N.Y. Sup. Ct. Jan. 23, 2013), Ex. A, 7, 9, 11, 18. One of the investors in the fund managed by RDLC was KBC Investments Ltd., a wholly-owned subsidiary of KBC Bank N.V., a premier Belgian bank. *See id.* ¶ 27. Between mid-2009 and mid-2010, the fund received redemption notices representing more than seventy-five percent of its capital, and it did not have enough cash to pay. Instead, it offered to pay in kind, by allocating certain assets into a liquidating account held for the benefit of the redeeming partners. *See id.* Ex. B, 4.

In 2011 and 2012, the KBC stake, worth about ten million dollars, was purchased by Paragon Outcomes and Ms. Irina Nevzlin Kogan. (Paragon subsequently acquired Ms. Kogan's interest.) *See id.* ¶¶ 27, 30-34. The problem with Paragon's stake, after different investors held separate stakes in different pools of litigation stakes, was that not all of those investments were successful. In particular, RDLC made a multimillion bet on a large pool of Vioxx cases which proved largely worthless. Redeemers, including Paragon, who happened to receive that very asset as part of their liquidation account, felt short-changed. The result was a dispute over which pieces of litigation-backed loans should benefit whom, and how to divide the losses. *See id.* Ex. C-E.

66. *See supra* Part II.B

67. John H. Beisner & Gary A. Rubin, *Stopping the Sale on Lawsuits: a Proposal to Regulate Third-Party Investments in Litigation*, U.S. CHAMBER INST. FOR LEGAL REFORM 4 (2012), www.instituteforlegalreform.com/uploads/sites/1/TPLF_Solutions.pdf.

68. Goral, *supra* note 60, at 13-14, gives an example of a case brought by plaintiffs represented by a law firm financed by an affiliate of the very institution which the plaintiffs sued for money.

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Market (AIM).[69] Money came from large institutional players: European mutual and pension funds, and insurers.[70]

From a funder's point of view, securing long-term capital by selling equity offers the luxury of patient investing (since investors can only withdraw money by selling their shares to someone else). In the context of litigation funding, it means that a funder can afford to bet on cases that may be highly profitable, but will likely take a fairly long time to resolve. And when liquidity is scarce, having capital locked up may be the difference between staying in business and closing shop (or never opening it).[71]

The downside of raising a permanent fund is the cost of capital. As soon as a fund is raised, the performance meter starts running for the entire sum entrusted by investors, putting the funder under pressure to quickly use the money in a productive

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69. Juridica Investment, Ltd. (using the ticker symbol JIL), was the first-mover, and it raised close to $200 million in two rounds. *See* JURIDICA INVESTMENTS, LTD., INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2009, at 8 (2009), http://www.juridicainvestments.com/~/media/Files/J/Juridica/pdfs/2009_Interim_Results.pdf (reporting shareholder equity of $196,694,515). Burford Capital, Ltd. (BUR) raised $300 million soon after. *See* BURFORD CAPITAL, LTD., ANNUAL REPORT 2010, at 14 (2011), http://www.burfordcapital.com/wp-content/uploads/2014/10/burford_capital_annual_report_web.pdf) (reporting shareholder equity of $295,827,000). Brokers specializing in corporate finance helped with the placements: Juridica used Cenkos Securities; Burford worked with Macquarie.

70. Institutional asset managers from Europe, mainly long-only funds. Major shareholders of Juridica include the asset management arms of Invesco (29.90%); Baillie Gifford (15.92%); AXA (8.99%); Jupiter (7.23%); and Milton Group (5.94%). *See Major Shareholders*, JURIDICA INVESTMENTS, LTD., http://www.juridicainvestments.com/investor-relations/financialdata-and-tools/major-shareholders.aspx (last visited Sept. 22, 2014) (listing shareholders as of March 31, 2014). Burford also lists Invesco as its largest shareholder (29.89%), but it appears to be more popular with hedge funds, including Eton Park (8.76%); Woodford Investment (7.23%); and Reservoir (5.57%). *See Share Information*, BURFORD CAPITAL, LTD., http://www.burfordcapital.com/investor-relations/share-informaton (last visited Sept. 22, 2014).

71. After Juridica and Burford had launched successfully, others tried to enter the market of high-stakes litigation funding. Those included BlackRobe Capital and Fulbrook Management (both founded by former principals of Burford and Juridica with the benefit of prior experience). It appears that a number of the new players had limited success in wooing investors and hence either failed to launch or operated on a very limited scale.

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way.[72] Even the most spectacular rate of return realized on an individual "litigation project" may be diluted to a negligible one if much of the money sits idly in a bank.[73]

A capital structure that minimizes liquidity challenges the evergreen model presents sets up a litigation fund as a "spoke" of a larger investment "hub"—for example, as a dedicated subsidiary of a large financial institution able to provide cash when needed and refer its own clients. However, in such a setting, the parent risks conflicts of interest interfering with its core business; and a transparent involvement in litigation finance may tarnish its reputation among peers. For those reasons, several investment banks, initially viewing litigation funding as a specialized financial service they were well poised to offer, ultimately chose to keep their distance.[74]

An alternative to raising a permanent fund is to take capital under the private equity model. Funders search for "limited partners" among high-net-worth and ultra-high-net-worth individuals or "family offices," in the United States and abroad.[75] Some actively solicit investments from around the globe, including the Middle East, East Asia, Israel, and Russia.[76] Many also enlist family and friends, and additionally invest their own wealth.

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72. The problem here is largely structural, and it does not quite go away after a funder commits most of his capital to identified investment targets. Unless a fundee pays for availability rather than actual utilization of capital, a funder needs to maintain fairly high levels of cash, commensurate to his commitments, which is costly. While it is possible to manage liquidity (i.e., reserve less than the total sum which the already closed projects may require, and account for cash returns from earlier investments), doing it efficiently is difficult due to uncertain maturities of "litigation assets" and the relatively small number of active positions which a funder keeps at a time.

73. For example, by the end of 2010, after one year in business, Burford reported that it had $230 million, or seventy-five percent of all its capital, parked in fixed-income assets (such as debt securities or money-market funds). *See* BURFORD CAPITAL, LTD., ANNUAL REPORT 2010, at 23 (2010), http://www.burfordcapital.com/wp-content/uploads/2014/10/burford_capital_annual_report_web.pdf. A year later, the amount dropped to about $145 million—just under fifty percent of the entire fund. *See* BURFORD CAPITAL, LTD., ANNUAL REPORT 2011, at 26 (2011), http://www.burfordcapital.com/wp-content/uploads /2014/10/burford_ar11.pdf.

74. Credit Suisse is a case in point. The bank had developed a reputable Legal Risk Strategies & Finance Group, which in 2012 was spun off as Parabellum Capital, LLC. Another funder operating in the United States as a specialized subsidiary is Bentham IMF, LLC, owned by Bentham IMF Ltd., an ASX-listed litigation fund with Australian roots. *See About Bentham*, BENTHAM IMF, http://www.benthamimf.com/about-us/bentham-imf (last visited Oct. 14, 2015).

75. For instance, Stillwater investors, introduced in *supra* note 64, included not only an English hedge fund acting through Belgian nominees, but also a sizable group of well-to-do Americans, including pensioners, hedge fund managers (investing personally), prominent lawyers, and professors at elite universities. While big investors, such as Eden Rock, invested tens of millions of dollars, the mean investment in the Stillwater Funds was $658,000. *See* Stillwater Plaintiff Memorandum, *supra* note 64, at 4.

76. Recall RDLF and Paragon Outcomes, and Irina Nevzlin Kogan, described in *supra* note 65. Paragon is a wealth management boutique catering to ultra-high net worth individuals. *See About*, PARAGON OUTCOMES, http://www.paragonoutcomes.com/#about (last visited Oct. 15, 2015). Kogan is a daughter of Leonid Nevzlin, a business partner of Mikhail Khodorkovsky in Yukos. Once one of Russia's richest men, Nevzlin and his family emigrated to Israel. *See, e.g.*, Courtney Weaver, *Leonid Nevzlin Is Biggest Winner from Yukos Ruling at The Hague*, FIN.

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While private-equity partnerships allow flexibility and privacy, and callable investor pledges help improve return on capital, money thus acquired must be returned when promised. If the funder fails to do so, or if investors decide that the funder did not perform as expected, investors may refuse to renew their commitments or renege on earlier pledges.[77] Therefore, many funders are on a permanent lookout for new investors, and their capital base tends to be a patchwork of different money sources and arrangements. Unlike large, closed-end funds, the "patchwork-funded" may allocate different portions of their portfolio, or even individual assets (that is to say, lawsuits) to different investor pools.[78]

Litigation financiers unable or unwilling to raise as much as they require in the form of equity leverage with debt. Much of that debt comes from debt funds and asset managers focusing on "alternative lending," or high-yield credit to enterprises underserved by traditional banks.[79] Some funders are also able to raise debt through securitization of their litigation-related holdings.[80] Leveraged debt is, at best, a medium-term source of capital, and it is usually quite expensive. Consequently, those third-party funders who use it look to invest in short-duration, high-yield "litigation assets," such as consumer advances, hoping to earn the excess spread.[81]

To summarize, third-party funders are constrained by their own funders. They need to subordinate their investment choices to the terms on which they obtained capital. Few can afford to bankroll large and expensive court wars. For example, if a funder's capital is in the form of three-year commitments, he will prefer fairly predictable investments expected to mature in medium term. Therefore, it would be

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TIMES (July 28, 2014, 5:20 PM), www.ft.com/intl/cms/s/0/bba18346-1669-11e4-a5c7-00144feabdc0.html #axzz3Du8iDClv.

77. *See supra* notes 64-65 and accompanying text.

78. Some funders would raise money on a case-by-case basis—which means that each lawsuit they invested in could have a different set of investors. Others, especially at the low-value, high-volume end, would sell "their paper" (meaning a bundle of litigation stakes) to a hedge fund looking to round up a larger portfolio with alternative assets.

79. *See, e.g.*, Ianthe Jeanne Dugan & Ruth Simon, *Alternative Lenders Peddle Pricey Commercial Loans*, WALL ST. J. (Jan. 7, 2014, 11:03 PM), http://on.wsj.com/19cxJhm (giving examples of investor-backed lenders catering to small business); Deloitte, Deloite Alternative Lender Deal Tracker: Focused on Primary Deal Flow in the European Mid Market, (2014), http://www2.deloitte.com/content/dam/Deloitte/uk/Documents/corporate-finance/deloitte-uk-altd-feb-2014.pdf (aggregating transaction patterns of thirty-two European alternative lenders and reporting increased capacity and versatility of non-bank funders).

80. 2011 saw a merger of Peachtree Financial Solutions and J.G. Wentworth, LLC, two financiers sharing their business between structured annuities and post-settlement litigation funding. Post-merger, they became controlled by JLL Partners, a private equity firm. *See* JGWPT Holdings Inc., Prospectus 7, 75 (Nov. 8, 2013). The Peachtree/J.G. Wentworth case is an interesting anecdote on who "owns" litigation funding business: as of June 30, 2013, the company had about $3.3 billion in securitized long-term debt, against $5.5 million in shareholders' equity. *Id.* at 24.

81. Companies providing litigation-related financing to consumers have been criticized for extolling very high interest rates from gullible individuals. Some of that criticism is valid. However, the high cost of financing should be kept in perspective. Critics rarely enquire into the cost of operations incurred by retail litigation funders, nor do they explain why many individual litigants cannot borrow more cheaply elsewhere, notably from a bank.

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more prudent for him to lend to contingency attorneys than, say, to bankroll an antitrust lawsuit. In a similar vein, a funder capitalized through short-term, high-interest debt will probably look to lend on even shorter and more expensive terms, perhaps focusing on the consumer market or post-settlement advances. Which suits a third-party financier is able to fund, and how, depends not just on how much money he has, but also on where the money has come from.

D. Lawyers

Of all the groups of actors engaged in the practice of third-party litigation funding, attorneys are the most interesting and the most diverse. They go far beyond the limits of what has been the traditional role of a lawyer, and wear many hats. One way to systematize what attorneys do in the context of litigation finance is to think about the stake they hold in the funded dispute. Borrowing from the stakeholder theory of organizational management,[82] attorneys can provide a service, manage somebody else's investment, or invest their own money.

First and foremost, lawyers provide a specialized, legal service. As litigators equipped with expertise and privileged status, they act as "litigation engineers": they put the facts together, evaluate them, and build a case for the represented client. Of all the actors, it is the lawyers who have the best information about a dispute and its variables, and they are best able to assess its merits and probable outcome.

But the process of investing in lawsuits also creates a demand for services other than litigation representation. Those services include transactional work, necessary to design and implement a financing arrangement. There, highly sophisticated legal advice might be required, since funding arrangements tend to be complex (they often need to accommodate interests of multiple parties, and may involve bespoke financial instruments, offshore jurisdictions, tax optimization considerations, etc.).

Another kind of service required in legal finance is legal underwriting—evaluating legal claims considered by a financier as an investment or collateral for a loan. Some funders have in-house teams of underwriters; others outsource the work (with many doing both). And it should come as no surprise that lawyers are often recruited as legal underwriters. Furthermore, some attorneys also act as legal brokers, referring potential fundees to funders, and vice versa.

In short, lawyers are capable of providing valuable services at different stages of the process aimed to extract value from ("monetize") legal claims: they help acquire the "asset," evaluate it, organize required financing, and enforce the claim—either in court or through negotiations. Such services may be highly sophisticated and expensive. Yet in all of the above roles, lawyers act as service providers. Their stake is similar to that of an employee: they supply labor as and when required by others and without much concern about the ultimate results their work helps accomplish.

But the ecosystem of American legal funding creates an opportunity, and sometimes a necessity, for attorneys to assume a different mantle—that of a manager.

82. *See, e.g.*, R. EDWARD FREEMAN, STRATEGIC MANAGEMENT: A STAKEHOLDER APPROACH 52-82 (2010).

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This is not to say that the managerial responsibilities of lawyers are confined to litigation funding. A partner in charge of a large case who supervises work of his team or coordinates with other specialists working for the common client is more of a manager than a jurist. Likewise, a modern general counsel who selects and supervises outside attorneys acts primarily in the managerial capacity.

However, the advent of legal financing has changed the job of a "legal executive"—also in litigation. On the one hand, the existing managerial roles increasingly require advanced financial skills, both for in-house and law-firm attorneys. In part, this has to do with the changes in how lawyers are compensated. The rise of the so-called "alternative fee arrangements," and bundled deals where legal advice in one matter is sold at a significant discount because the revenue lost can then be reclaimed elsewhere,[83] make the legal math and business planning more complicated.

On the other hand, the growing financial sophistication expected of lawyers has created demand for entirely new tasks and roles. In litigation, there are at least two such new roles; they may be called the "legal project manager" and the "legal asset manager."

As a project manager, an attorney sets out the tactics and marshals the resources necessary to achieve defined objectives of a legal transaction. To some extent, such a task has always been a part of the job of a billing partner—for example, she has been expected to assign younger lawyers with lower hourly rates to more menial tasks while utilizing more expensive senior lawyers for high-end work. But a modern manager of legal projects does much more. She defines specific objectives ("deliverables") and outlines measurable milestones to be reached on the way to the goal. She tries to optimize the process with regard to scope, time, and cost. And she manages the risk, also by knowing when to walk away from the table—or from a court.

In litigation, a rigorous, managerial treatment of a case is a fairly new concept, not always easy to implement. Defining even the most basic financial parameters of a legal dispute, such as its expected value, cost, and time to resolution, often proves challenging.[84] Deciding how those parameters should be adjusted in midstream, based on developments in the case, is just as tricky. But there clearly exists a growing demand for lawyers able to use tools and methodologies developed for managers working on other kinds of investment projects.

The demand for legal project managers is both internal and external. Law firms need them because misjudging how much work a case may require, how long it

83. *Cf.* Goral, *supra* note 60, at 17-24 (studying the idea of case bundling in the context of complex litigation and informal aggregation of related cases). For a discussion on the relationship between alternative fee arrangements and "commercial" litigation funding, see Radek Goral, *Skin in the Game: Why Business Lawsuits Get Third-Party Funded*, 30 NOTRE DAME J.L. ETHICS & PUB. POL'Y (forthcoming 2016).

84. Many financiers I interviewed complained that even seasoned, successful litigators struggle when required to design, execute, and report on case management in terms of a budget and other financially relevant objectives. *See* Goral, *The Law of Interest*, *supra* note 30 (manuscript at 32-33, 53-55).

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should take, or how much it could cost, will impact their bottom line. This is especially true when the ever more popular alternative fee arrangements cap attorney's fees for a specified scope of work or tie compensation with preset deliverables. Relatedly, attorneys may have their performance evaluated based on a concrete metric which those who control the purse strings (third-party funders before all) find more pertinent than the lawyer's subjective impressions on the progress of a dispute or its outlook.

The same logic applies to general counsel, constrained by a budget and answerable to executives who may lack legal background, but who are used to thinking in terms of project execution. Interestingly, when it comes to corporate disputes, some outsource the required legal work as well as the specialized managerial function; however, the litigator and the manager are not necessarily the same person.

While external managers may supervise litigation purely for efficiency, some empirical evidence suggests that they feature especially in those disputes where the legal claim and resources for its prosecution come from separate places.[85] In funded litigation, it is not uncommon for a lawyer-turned-project manager to act next to one or many litigators—formally, as co-counsel; substantively, as the litigation equivalent of a general contractor, a link between the owners of a disputed claim and those in control of the capital and skill required to extract the claim's value.[86]

A litigation project manager takes care of the financial and organizational aspects of a specific dispute. But the commoditization of legal claims has created another managerial role, requiring focus on multiple "legal assets" at the same time. The person entrusted with that responsibility, called here a legal asset manager, is in charge of a portfolio of valuable litigation stakes, and usually, his goal is profit maximization.

The above job description is essentially what third-party funders do for investors interested in betting on litigation in a systematic way. There are also those who have been running "proprietary trading desks" of litigation interests for many years, including the entire breed of contingency lawyers. Recently, however, law firms traditionally charging by the hour have resigned themselves to success-based compensation or "performance bonuses." This left them with multiple, and often diverse, contingent stakes in the matters of their clients, acquired in lieu of the forgone hourly billing. Such firms, and some affluent and forward-thinking plaintiff attorneys, seem to appreciate that a pool of uncertain, future earnings may become either an important source of revenue or a major threat to cash flow, and that it must be tended to with discipline and structure.

That last remark brings about the third kind of stake which lawyers may have in in the context of litigation finance: a lawyer may wear a hat of a litigation investor

85. *See* Goral, *supra* note 60, at 17-20 (providing a real-life anecdote of a law boutique founded by two partners who quit an AmLaw 100 firm, and the law boutique's role as the litigation manager in a prominent antitrust case).

86. A particular type of litigation project manager takes the form of a special-purpose law firm. Such an ad-hoc vehicle can be a formalized way to allocate work and stakes among a number of firms contributing work and/or money.

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and own an economic interest in a legal dispute. Apart from holding a stake in a client's claim acquired as an attorney's fee, there are two special cases of attorney ownership stakes. Those may be thought of as two extremes of a continuum distributing lawyer stake-holding in legal claims based on the parity between the lawyer's input of labor and capital.

At one end of the spectrum there are "banker lawyers," whose contribution in a case they formally represent is essentially limited to cash. While banker lawyers often act as counsel to a claimholder, they sit at the table to keep an eye on their "asset" rather than to offer additional legal advice.[87] Banker lawyers are investors and legal asset managers in one, using their insider status as attorneys for a competitive advantage.[88]

At the other end of the continuum are law firms holding ownership stakes as fiduciaries. They serve as qualified investment vehicles adorned by a façade of a legal practice that provides actual economic stakeholders with an opportunity to bet

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87. "I served as chief counsel to [a large public institution] and I saw defendants facing those special-purpose law firms," recalled a litigation partner in a defendant law firm I interviewed. "Behind them were so-called 'banker lawyers.' Who are they? Very rich lawyers who are not active in the case . . . . [who, for example,] made money on asbestos litigation and bankroll other lawyers."

88. One of the most notorious cases discussed in the context of litigation funding is that against Chevron, sued for the alleged environmental damage caused by its subsidiary drilling for oil in Ecuador's Lago Agrio region. *See, e.g.*, Simon Romero & Clifford Krauss, *Ecuador Judge Orders Chevron to Pay $9 Billion*, N.Y. TIMES (Feb. 14, 2011), http://www.nytimes.com/2011/02/15/world/americas/15ecuador.html?_r=0 (reporting on the $18 billion judgment against Chevron entered by the trial court in Ecuador); Patrick Radden Keefe, *Reversal of Fortune*, NEW YORKER (Jan. 9, 2012), http://www.newyorker.com/magazine/2012/01/09/reversal-of-fortune-patrick-radden-keefe (discussing the dispute, behind-the-scenes maneuvering, and its ethical ramifications). Buford, introduced in *supra* notes 69-71, invested in the *Chevron* litigation, and details of the investment have become public. *See* Supplemental Declaration of Kristen L. Hendrick at Ex. B, Chevron Corp. v. Donziger, No. 11-cv-691 (S.D.N.Y. Nov. 29, 2011), ECF No. 356 (the funding agreement between Burford's subsidiary and representatives of Ecuadorian claimants) [hereinafter Chevron Litigation Funding Agreement]. Critics have unfairly presented the case as a poster child of litigation funding. *See, e.g.*, U.S. CHAMBER INST. FOR LEGAL REFORM, *supra* note 67, at 4-6 (using the case to argue that litigation funders back risky cases of dubious merit). The publicity also lured scholars to use the outlier case as an anchor for more general scholarly vagaries. *See, e.g.*, Maya Steinitz, *The Litigation Finance Contract*, 54 WM. & MARY L. REV. 455 (2012).

For the purposes of the discussion at hand, *Chevron* is an anecdote on how the new wave of dedicated commercial funders relates to banker lawyers as market incumbents. Specifically, Burford came to play only in the third act of the *Chevron* drama. It was not the first, nor the largest (in terms of deployed capital), third-party funder engaged by the plaintiffs and their lawyers. In fact, Burford was able to make a deal only after the original funder closed his purse. That funder was a banker lawyer: Joseph Kohn and his law firm, Kohn Swift & Graf P.C. *See* Chevron Corp. v. Donziger, 768 F. Supp. 2d 581, 597 (S.D.N.Y. 2011). According to the defendant's legal team, until 2010, Mr. Kohn and KSG invested in a systematic and structured fashion, injecting more than $7 million in the case. *See* Amended Complaint at ¶ 328-30, Chevron Corp v. Donziger, 2011 WL 1805313 (Apr. 20, 2011), ECF No. 283 [hereinafter Chevron Complaint].

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on and influence legal disputes under the aegis of law and privilege available to attorneys.[89]

To recapitulate: the central role of attorneys in the third-party litigation funding stems from their substantive expertise, their position as accepted market incumbents, and their ability to channel investible capital to investible legal claims. Those qualities give lawyers a competitive edge, making them suitable for various roles in the ecosystem of legal finance. In a funded dispute a lawyer may be a litigator, or provide another type of service; but she may also act in a managerial capacity, or behave primarily like a capitalist looking after her investment.

E. "Entourage"

In the ecosystem of legal finance, like in any burgeoning business industry, next to major stakeholders there is also a place for actors with ancillary roles. The "entourage" provides a range of valuable services, including intermediation, investment valuation, and data analysis.

One important group facilitating the funding business is litigation brokers, or "case hunters." Some are free-lancers; others work in-house. Their job is to acquire attractive clients—litigants or lawyers—for the funder willing to pay for intermediation.[90] This includes targeting fundees already attached to another financier, in an attempt to win them over for a competitor. Although case hunting attracts people with various backgrounds,[91] there are many lawyers among them, including active litigators willing to tip off a friendly financier about a colleague or client in need of cash, in exchange for a quick referral fee.

Another kind of specialist supporting at least some funders are financial consultants. Some of them, such as The Claro Group,[92] or Finance Scholars Group (recently acquired by Claro),[93] have teams specializing in modeling and estimation of litigation-related economic parameters, such as damages or costs. Consultants also

89. *See* Goral, *supra* note 60, at 17-20 (giving examples of such arrangements).

90. Brokerage fees are often viewed as transaction costs, passed on to the fundee.

91. According to an anecdote shared by industry insiders, a large commercial funder was approached by a broker from Southern California (a former star of the adult entertainment industry). Like a matchmaker, she offered the funder a group of attractive, though cash-strapped, cases in need of a resourceful partner. Skeptical about the broker's credentials and worried about its own image, the funder refused to negotiate. In hindsight, that decision turned out to be hasty. The broker turned to the funder's competitor who, concerned only with the potential of the cases offered, snatched them without much ado.

92. The Claro Group has a separate Disputes, Claims and Investigations Consulting Practice, focused on economic aspects of insurance claims, litigation finance, and bankruptcy. *See Disputes, Claims and Investigations*, CLARO GROUP, http://www.theclarogroup.com/home-2/dispute-claims-investigations (last visited Oct. 8, 2015) (claiming expertise in "issues that arise in the marketplace and in business litigation," related to accounting, economics, and valuation).

93. *See Our Expertise*, FIN. SCHOLARS GROUP, http://www.fsgexperts.com/our-expertise (last visited Oct. 8, 2015) (claiming expertise in "issues that arise in the marketplace and in business litigation," related to accounting, economics, and valuation).

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help funders develop methodologies used in investment valuation and accounting applied to legal claims.

There are also those who, like Stanford-born Lex Machina, provide quantitative data on litigation. The startup tries to marry legal research with computer science in order to provide what it calls "legal analytics" for patent litigation—it mines and crunches case records to find patterns in how particular parties, lawyers, or judges behave, or how patent cases fare depending on the district or even the judge hearing the case.[94]

The providers of ancillary services used in litigation finance are often young, quickly-evolving ventures. While it is difficult to predict what the future has in store for many of them, the "entourage" actors deserve special mention because their work tends to be innovative. Applications of such work often transcend the practice of third-party litigation funding, and they may prove valuable for a broader audience of litigation practitioners.

IV. Market Fragments, or Different Ways to Bet on Suits

Legal claims vary dramatically and along many dimensions. A "litigation investment" could mean a stake in a legal claim of monetary value, a tangible or intangible asset whose ownership gives certain legal rights against others (a share, a piece of real estate or patent), a collection of claims or assets, or a going concern the revenue of which comes from a systematic pursuit of legal claims (also known as a litigation law firm). Consequently, from the point of view of a financier, litigation is not one asset class, but many; and multiple ways exist to invest in them.

Depending on the risk they are ready to assume and the reward they expect, third-party financiers focus on different segments of the legal market. What (and whom) they fund determines how they do it. How powers and responsibilities are shared between the funder and the fundee depends on a particular financing approach. The relative power of parties impacts their respective risks and benefits. Using those three pairwise dependent variables—funding target, risk, and control—this Part overviews different segments of the American litigation funding market.

A. Who Takes the Money

The most broadly accepted taxonomy of the market for litigation funding in the United States seeks to segment it based on who receives the money. Therefore, the classification distinguishes: (a) "consumer funding," directed at individual plaintiffs; (b) "commercial funding," where a funder provides capital required to prosecute a business claim; and (c) "law-firm funding," which consists of providing capital to attorneys.[95]

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94. *See What We Do*, LEX MACHINA, https://lexmachina.com/what-we-do (last visited Oct. 15, 2015).

95. *See* Garber, *supra* note 5, at 1, 9, 13. For recent works which seem to follow Garber's taxonomy, see, for example, Burch, *supra* note 2, at 1301-04; Engstrom, *supra* note 3, at 383; and Pardau, *supra* note 3, at 67.

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Other than stating that some fundees happen to be consumers, corporations, or law firms, the tripartite division reflects how litigation financiers sometimes see themselves in relation to their peers, giving an idea of the funder's main clientele. It is also a shorthand for a funder's position in the market.

1. Consumer funders

The consumer segment represents the low end, with fairly simple, generic transactions. It is a low-value, high-volume business, where the funder is able to build a pool comprising many thousands of stakes in consumer claims, usually worth a few thousand dollars each. Those stakes tend to be similar in nature (largely, but not exclusively, personal injury), so that the financier is able to diversify unsystematic risk by putting to work the law of large numbers. This kind of business is about size, rather than sophistication. Consequently, a consumer financier relies largely on marketing and an ability to manage large-scale operations.

2. Commercial funders

Commercial financiers occupy the other end of the market. They select a relatively small number of stakes, rarely more than a few dozen at a time, but the bets are large—from a few hundred thousand to tens of millions of dollars per investment. Because portfolios of commercial funders are typically too small to be well-diversified, their success depends on how well they select assets. This means that evaluating and managing cases is far more proactive (and costly) compared to the consumer segment. Transactions are bespoke and individually negotiated.

3. Law-firm funders

The law-firm segment is in between the two ends, and it is quite diverse. Some funders manage only modest portfolios, while others can easily compete with their commercial counterparts in terms of investment capital and transaction value. Screening and management of investments is rigorous and involved. Products offered tend to be typified, but somewhat negotiable. And, like in commercial funding, clients are businesspeople.

It is tempting to assume that the sets of *fundees* and *funders* are one-to-one: that is, that for a fundee of a given kind—consumer, commercial, or law-firm—there is one corresponding kind of a financier. Such assumption would not be true, though: commercial funders deal with corporations, but may also back law firms, or even individuals (although usually ones acting in a business capacity). Law-firm financiers, who cater primarily to lawyers, sometimes also fund those lawyers' clients, or pay for personal expenditures of individual attorneys and their families (such as mortgage or auto loan payments, insurance premiums, professional membership fees, or children's school tuition).

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Furthermore, contrary to suggestions by some scholars,[96] a particular category of a *fundee* or *funder* does not map easily to one model of *funding*. Litigation stakeholders may be funded in different ways, with one provider offering several types of service. Therefore, the division into consumer, law-firm, and commercial segments should be taken as a quick-and-dirty way to distinguish financiers based on the primary clientele they target.

When it comes to who gets the money, the main qualitative line of division runs between consumers and businesspeople. Financing offered to consumers is narrow in business terms: it usually involves advancing money against expected proceeds from legal claims (at different stages of case development). Here, funders complement services of contingency lawyers because third-party money is almost always used to pay for personal expenses of the consumer litigant, which attorneys are not allowed to finance.[97] At the same time, funding consumer litigants involves serious normative questions, as consumers have a special, legally protected status.

In contrast, commercial and law-firm funding both encompass diverse transactions between profit-oriented professionals. Both provide capital which, for the most part, is used to develop litigation stakes of the fundee—both are a capital investment in a legal claim, rather than a way to pay for the consumption of the claim's owner. Additionally, the distinction between funding directed at professional litigators and investments targeting their clients is sometimes blurred. Sometimes both are two sides of one coin.

4. Who takes the risk

That different kinds of investments in legal claims have different risk profiles is a central tenet of third-party litigation funding. When a funder bets on lawsuits, he tries to choose strategically, from among the "assets" with risk-reward profiles matching his appetite. The problem is that investment risk presented by a legal dispute is difficult to measure; and evaluating it in a reliable, systematic, and cost-effective way, especially without accessing privileged insider information, is even harder.

The market has addressed the problem of risk discrimination with a rule-of-thumb approach. In practice, the domain of investments in legal claims is stratified along a straightforward, easily observable variable which, by and large, correlates well with litigation risk: the stage of life of the underlying legal claims. Based on that criterion, financiers distinguish pre-settlement, appellate, and post-settlement funding.

Dividing legal cases based on how far down the road to money they might be helps funders with risk-conscious selection of suitable investments. But, by itself, it

96. For example, Garber, *supra* note 5, at 1, incorrectly asserts that consumer funding consists of non-recourse lending to consumer "plaintiffs with pending lawsuits" and law-firm funding (in "subprime lending to plaintiffs' law firms" handling personal-injury cases), and that commercial funding should mean investing in commercial "lawsuits or their proceeds." Others repeat that framing. *See* sources cited *supra* note 95 (citing sources).

97. *See* MODEL RULES OF PROF'L CONDUCT r. 1.8(e) (AM. BAR ASS'N 2011) (prohibiting lawyers from financially assisting clients, save for court costs and litigation expenses).

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does not explain how to take a position in the desirable kind of litigation assets. As it turns out, the market has developed funding strategies considered standard for a given partition of legal risks. In effect, when financiers talk about pre-settlement, appellate, or post-settlement investment, they have in mind one or several transaction types characteristic for that stage.

5. Funding pre-settlement (early stage)

The first partition of litigation risks comprises "young" cases—those not yet resolved (and sometimes, yet to be formally commenced).[98] Since facts or law relevant for the outcome remain unknown or undecided, such disputes are subject to substantial uncertainty and are considered high-risk. Their evaluation requires case-specific expertise, which results in relatively higher transaction costs. Furthermore, average life expectancy of young cases is high, which implies a long holding period for a third-party investor.

While some financiers are ready to bet on risky, early-stage claims, they usually do not want to assume the full risk of an individual case going south. Practical solutions to that dilemma are twofold. First, a financier can bet on more than one claim at a time—hoping that even when some claims do not pan out as expected, others will do well, rendering the entire investment profitable. The second solution is the scope of the funder's recourse: his payout may be limited to the outcome of the disputes on which he bet. Or the fundee may remain liable to the funder even in the event that the claim at stake does not fare as expected.

Based on the number of assets covered by a single investment and the scope of the funder's recourse, three distinct strategies of pre-settlement investing may be identified: (1) a full-recourse, portfolio-wide financing, (2) a non-recourse, limited-portfolio bet, and (3) a non-recourse, single-asset funding.

(1) *Recourse cash-flow financing:* The safest practical way to bet on risky, early-stage legal claims is to bet on a whole pool of such claims *and* have a recourse against the fundee also in the event that the funded claims are not resolved as hoped. To implement such strategy, a funder needs a repeat-player counterparty—someone with a large, preferably renewable, pool of litigation assets. This may mean a large corporation whose business generates a steady stream of litigation work. In practice, however, litigators prove to be more viable partners for a litigation funder, primarily those working on contingency and in constant need of working capital. Hence, the portfolio-wide, recourse financing usually takes the form of law-firm loans.

Pre-settlement funders typically invest in a law firm as a going concern: they provide capital against the cash flow which the legal practice is expected to generate over the life of the investment. A funder provides working capital required by borrowing attorneys to prosecute cases—ordinarily, in the form of a line of credit on which a fundee draws to pay case expenses and, sometimes, also operating costs of

98. Any investment made before a claim is decided is considered "pre-settlement," even though the risk associated with the same dispute at the filing of a complaint and right before its resolution would normally be very different.

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her business. The loan is full-recourse, which means that the funder is secured on all assets of the borrowing law firm, as well as personal assets of its senior partners.

The wide collateral notwithstanding, law-firm loans are normally meant to self-liquidate: the primary source of repayment is the firm's inventory of cases, and the revenues which the attorneys expect to earn from the inventory. Both the financing and the collateral are dynamic: the fundee borrows as needed up to a limit; and her lawsuit portfolio securing the funder changes over time as she resolves some disputes and signs new clients. Therefore, the funder is in a position similar to that of a secured creditor of a producing business.[99]

Law-firm loans are the domain of "law-firm" financiers, but they are also offered by "commercial" funders, sometimes as a way to manage excess cash temporarily not invested elsewhere.

(2) *Nonrecourse, multi-asset financing:* Under this model, the financier invests on the limited-pool basis. Here, he stands to profit from a successful outcome in any of the disputes covered by the deal, but from nothing else. In particular, there is no recourse to personal net worth of the fundee.

Like full-recourse lending, the logic of limited-pool transactions dictates that fundees have multiple lawsuit stakes on their hands. Suitable targets for limited-pool funding include plaintiffs with several, often related, claims against multiple parties.[100] Or it may be directed at law firms. Today, nonrecourse, multi-asset funding is primarily a province of large, "commercial" funders, banker lawyers, and deep-pocket patent investors.[101]

In a limited-pool transaction, the funder's interest in the pool may be a straight percentage of the pool proceeds; but more often, such interest is nonlinear and expressed by a more complex formula. The financier usually has a priority return on the proceeds from any of the cases in the pool, which helps him spread the risk.[102]

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99. The true nature of a pre-settlement financing may be more complex than its designation as a loan suggests. At times, the funder behaves more like an equity partner than a passive creditor, because he obtains broad discretionary powers over how and when his money gets spent and because attorney loans are renegotiated when the situation of the parties changes.

100. For example, a manufacturer may fund its claims against all members of a price-fixing cartel; a policyholder could pool claims against several insurers with participations in liability for an accident. One substantive area where claims grouping is especially prevalent is intellectual property: related patents are routinely bundled into portfolios that cover a set of functionalities used in market products of a certain type. When such patent bundle is to be monetized through third-party funded litigation, the funder will take a stake in multiple rights (or even multiple bundles) to be asserted against multiple infringers.

101. Burford after it lost money on a patent bet, informed investors that "while patent wins can be disproportionately large, there is also a greater risk of . . . . unanticipated loss than in other types of litigation, and we are generally more comfortable taking patent litigation risk only on a portfolio basis." *See* BURFORD CAPITAL, LTD., ANNUAL REPORT 2012, at 13 (2013), http://www.burfordcapital.com/wp-content/uploads/2014/10/2012-FY-Results-Burford-Capital-Annual-Report-TEMP.pdf; *see also supra* notes 69-71, 88. Burford's main competitor, Juridica Investments, embraced the multi-asset approach right from the outset, with respect to both claimants and law firms. Other commercial financiers also fund on the pool basis.

102. Assume, for example, that the financier funds three independent cases, each expected to generate $1 million in proceeds. In exchange for his money the financier stands to earn $0.4 million, but not more than 50% of proceeds actually collected from each of the three suits.

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This in turn benefits the fundee, who is able to acquire capital on better terms than financiers would be willing to offer when investing on a case-by-case basis.

While parties have much freedom when arranging multi-asset financing directed at claimholders, transactions involving limited pools of attorney's fees are more challenging because of the fee-sharing prohibition.[103] Funders and fundees tend to work around it by structuring the deal as a non-recourse debt,[104] and by arguing that recourse limited to fees from a few cases leaves the attorney with enough wiggle room so as not to tread on her independent professional judgment.[105]

(3) *Nonrecourse, single-asset financing:* The most risky variant of legal financing consists in betting on a single case, without recourse to anything other than a portion of uncertain, future proceeds from the one dispute.

Such "equity investments" in litigation stakes differ in substance and structure. They are most suitable for high-stakes business suits with enough at stake to leave the fundee, and often also the attorney, with "skin in the game" after the third-party financier takes his share of the proceeds. Given the risk involved, the funder's share tends to be large, sometimes as high as fifty percent. Like in limited-pool transactions, the funder may be promised a simple percentage of the future proceeds or parties may agree to distribute money in a more sophisticated way, not unlike in private-equity deals.

Now suppose that the first case settles for $0.5 million, the second is lost entirely, and the third is resolved for $2.5 million. If cases are funded on a case-by-case basis, the funder would receive $0.65 million: $0.25 million from the first case (due to the 50% constraint); $0 from the second case; and $0.4 million from the third. If he funded the same three cases on a pool basis, the financier would stand to earn 3 x $0.4 million = $1.2 million, but not more than 50% of the total proceeds from the pool. For the same case outcomes of $0.5 million, $0, and $2.5 million, the pool would generate $3 million. The financier would then receive $1.2 million (which is less than 50% of the pool)—almost twice as much as under the case-by-case arrangement. In short, the pool-wide funding diversifies unsystematic risk. In the example above, despite the high variance of outcomes the pool yields the mean expected return of $1 million per case.

103. *See supra* Part II.C

104. The financier's return on the case (pool) is often subject to a double, the-lesser-of-the-two, kind of constraint: the accrued, interest-like return, inflated by a high nominal rate; and the scope of the financier's recourse. Suppose, for example, that a financier extended $1 million to a firm against $3 million the firm expects to earn in fees. The financier's return accrues at the annual rate of 40%, but his recourse is limited to 50% of the attorneys' fees actually collected. If the fees are paid as expected after one year, the law firm will pay the funder 40% x $3 million = $1.4 million. If the fees were paid after two years, then the principal would accrue $1 million x $(1.4)^2$ = $1.96 million. But since the limit of recourse was fixed at 50% x $3 million = $1.5 million, the financier would only receive that latter amount, which is economically equivalent to one-half equity stake in the attorney's fees.

105. Here, funders and their law-firm partners walk a fine line. It appears that the question of how many assets must be in a pool of fees to comply with Model Rule 5.4 is case-specific and cannot be answered with a number. Much will depend on the relationship among the pooled cases, as well as the significance of the pooled fees for the funded firm.

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6. Funding appeals (medium stage)

This in turn benefits the fundee who can acquire capital on more favorable terms than financiers would be willing to offer when investing on a case-by-case basis.[106] There, the funder's interest attaches to non-final judgments (or other forms of legally binding, but appealable adjudication) awarding something of value—after the adversary challenged the judgment.

Funders see the appellate review as a playoff round in a lengthy judicial process, after relevant facts have been discovered, and value of the case established. An appellate investment involves additional litigation risk, but when compared to pre-settlement disputes, appeals are perceived as easier to assess in terms of identifiable risk factors, time, and cost (largely limited to additional attorney's time).

A third-party investing at the appellate stage purchases an interest in a judgment either from the plaintiff or her attorney. Sometimes, the funder's interest in the judgment is a pure equity stake in the challenged award; at other times, it increases with time. In any event, an appellate funder bets on appellate cases one by one, and his recourse is limited to a share of the individual judgment purchased—as long as it survives the appeal.

7. Funding post-settlement (late stage)

The equivalent of a late-stage investment in the litigation context is the post-settlement funding. It is a special kind of bridge financing, addressing the gap between the time of a lawsuit's resolution and the time when the amount of recovery is actually disbursed to the plaintiff or her lawyer. In many ways, the post settlement funding is akin to traditional factoring of receivables.[107] Since the legal disputes suitable for post-settlement funding have already been finally resolved, the funder advances money against proceeds which by then are earned but not yet satisfied by the losing party, at a discount commensurate with the risk that they will not be paid on time.

The post-settlement model involves little uncertainty, because the quality and value of legal claims has already been ascertained at this stage. What remains is the counterparty risk (the chance that the defendant will default), although cases where

106. Strictly speaking, an appellate case is a pre-settlement risk. Conversely, a pre-settlement investment may pertain to a dispute where the outcome is appealed. Hence, it would be more correct to describe early-stage investments as "pre-resolution" or "pre-judgment." Moreover, both pre-settlement and appellate "assets" ultimately reach the post-settlement stage (unless lost). The "pre-settlement," "appellate," and "post-settlement" nomenclature comes from funding practice and, like most of the practice-derived concepts, it is not very precise. However, since it has acquired a life of its own, I accept it for the purposes of this paper as part of litigation funding ethnography.

107. The proceeds of a finally resolved case owed to the plaintiff (and from the plaintiff to her lawyer under the contingency fee agreement) become bookable assets—accounts receivable. They are either assigned to the financier for collection purposes, usually with a full, subsidiary recourse (in case the defendant fails to make good on the award or settlement, the financier has the right to demand payment from the plaintiff), or used as a low-risk collateral of a bridge loan extended to the plaintiff.

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the depth of the defendant's pockets is in serious question are not very likely to be financed. In addition, the expected time to payout in post-settlement cases is much shorter than in a pre-settlement ones. Such investments are also much easier to describe in quantitative terms, without an intolerably high risk of measurement error or dubious statistical assumptions.

Some post-settlement transactions involve an individual claim; others comprise a pool of lawsuits, and the funder then earns a return from whatever is collected on the entire portfolio. Non-recourse post-settlement financing dominates in the market: the funder assumes the risk of the obligor's (the losing litigant's) default. At the same time, the funder is usually protected—up to a point—from the risk that the obligor would pay late, because his return, like that of a lender, tends to be time-dependent.

In terms of fundees, this type of financing is offered to plaintiffs (primarily individuals) as well as law firms anxious to cash their fees. The two often go hand-in-hand, with the same financier backing both the settling plaintiff and her attorney.

B. Who Takes Control

Apart from who gets the money, and who carries the risk, one more dimension that helps systematize litigation-related investments is the level of influence which the third-party investor obtains in the case he bankrolls. Although many funders seem keen to present themselves as "strictly passive investors," how much of a say they really have varies significantly. Therefore, we can distinguish passive investments; those which are actively managed by the funder; and stakes in which his word is last.

1. Passive stakes

When a funder acquires a passive stake in a legal dispute, he takes a "hands-off" approach to the case after making an investment, leaving decisions to other stakeholders—normally, the claimant and her attorney. For some investing strategies, this passive approach is preferable—especially when the nature of the stakes acquired by the funder are too low or too numerous to make a hands-on approach practicable. Advances to consumers are usually passive. So is post-settlement funding, for the simple reason that there is little left to manage in a case once it is finally resolved.

Appellate investments, too, often leave little room for active involvement by a funder who comes into an already well-defined dispute, where he either buys an "as is" stake or he does not. On the tactical level, appellate cases usually pivot around specific points of law, best left to attorneys specializing in appellate litigation. (However, appellate financiers, as real parties in interest, usually have a say in settlement negotiations.)

As a rule, recourse law-firm loans should also be considered passive, because the lender generally does not get involved in how a fundee firm handles its case inventory. On the other hand, he does monitor how the firm performs financially—whether its cases are resolved as expected, and whether it takes and pays out money as agreed. The funder, or his affiliate, may also act as a financial adviser to the funded firm. And if the fundee gets in trouble due to mismanagement or bad luck, the financier has enough leverage to exert significant influence on the funded practice as a whole.

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2. Actively managed stakes

When a third-party funder invests in business-to-business claims during the pre-settlement stage, either individually or on a limited-portfolio basis, he is engaged in their management to a degree. (This also applies when the limited-pool fundee is a law firm.) Such investments are made early in the life of a dispute, and normally there is much left to be done, with stakes high enough to justify careful planning and execution. The level of involvement by a funder is case-specific, and it pertains to both legal and extralegal aspects of the case.

When it comes to litigation strategy, funders may wield significant influence. Their tools include the funding agreement, which often sets conditions precedent on effecting any funding or links financial incentives to a detailed course of action to be taken in the case.[108] Or the deal might provide for a funder's trusted attorney to be appointed by the funded litigant as "liaison counsel," giving the funder a seat at the table in all but name.[109] The primary source of funder's influence is economic, however: it comes from his discretionary power to discontinue funding in midstream, potentially forcing abandonment of the case. The control of the purse strings means that it is not rare for litigants—and sometimes their attorneys—to seek a funder's approval for strategic decisions in the case, even when such approval is not formally required under the funding contract.

Outside of the litigation process in the narrow sense, funders are involved in various initiatives which improve the chances of enforcing the funded claim. In certain cases, they undertake orchestrating a public-relations campaign, advise on financial issues (such as estimation of damages or structure of payments under settlement), recommend experts, or identify assets owned by the adversary expected to fight enforcement of adverse judgment.[110]

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108. For example, "commercial" funders universally contend that they always leave settlement decisions to the funded litigant. What they do not say is that the fundee's choice may be economically constrained. For one, under some funding contracts, parties would put a numerical value on the case and link the funder's minimum return to that value unless waived. In economic terms, the fundee then writes the funder a put option on the settlement actually accepted by the fundee without the funder's consent (and waiver) with the contractually agreed-upon case value operating as a notional for the put's strike price.

109. In the Ecuadorian case against Chevron funded by Burford, mentioned already in note 88 above, the funder appointed as liaison counsel Patton Boggs, LLP, a firm working closely and repeatedly with the funder. Patton Boggs was to monitor and authorize all disbursements from the funds made available by Burford. *See* Chevron Litigation Funding Agreement, *supra* note 88, at 1.32-33, 2.1-.4.

110. In *Chevron*, Burford and its lawyers prepared a memorandum titled "Invictus," which detailed a wide array of extra-legal steps to be taken, including a "media push," filing "personal injury lawsuits in the United States," a detailed strategy of international enforcement, a plan to frustrate Chevron's strategic acquisitions, and diplomatic steps meant to bring the government of Ecuador "into the fold." *See* Declaration of Kristen L. Hendricks at Ex. 341, Chevron Corp. v. Donziger, No. 11-cv-691 (S.D.N.Y. Feb. 6, 2011), ECF No. 49, at 17-23, 28-29. Chevron lawyers claimed that the memo was penned by Patton Boggs, acting at Burford's behest. Chevron Complaint, *supra* note 88, ¶ 331.

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3. Majority-owned stakes

There exist commercial cases where the funder has effective control over a dispute in which he invests. In particular, a funder can acquire title to an asset underlying the legal claim to be monetized (such as a patent, stocks, or real estate). Or he might be assigned certain alienable claims even if they do not emanate from another asset (claims in bankruptcy or insurance claims acquired by way of subrogation are good examples).

In all of the above situations, the funder has free rein to direct the enforcement of the majority-controlled claim, sometimes from before a suit is filed. The funder then assumes the mantle of a litigant and makes all strategic decisions in the case—from the selection of lawyers, to directing them without compromising the attorney-client privilege, to settlement.

The original claimholder then becomes a passive party, and her rights in litigation are limited to a share of proceeds and such other rights as the funder promised under contract. It should be noted that having a funder at the helm may be convenient for the fundee who may be anxious to be rid of the claim, does not feel competent to manage the enforcement herself, or would rather that someone else be the face of a dispute for reputational reasons.

V. Meet the Funders

The picture of companies providing money to litigation stakeholders is a colorful mosaic of business models, practices, and personalities of the people who have founded and continue to manage those companies. Virtually no two of those are the same, which makes any attempt to label them based on clearly delineated criteria rather challenging—even more so because most companies offer several types of services.

Part III positioned funders within a larger ecosystem of litigation finance. Part IV took a peek at what funders do, and the many different ways in which third-party money reaches legal disputes. Here, I identify specific companies funding American litigation—it is time to meet the funders.

A. Funders Large and Small

Third-party funders of litigation are portfolio managers—they allocate capital entrusted to them by investors into a number of litigation-related assets. One of the most important metrics of an investment portfolio is its size, or the fair value of the pooled assets (including spare cash), commonly known as the assets under management (AUM). Size matters—how a fund manager invests depends, among other things, on how much money he has.

In AUM terms, law-firm funders can be arranged into a spectrum. At the lower end, there are small private providers whose funds range from a few to mid-teen millions of dollars. Some of them self-deprecatingly call themselves "mom-and-pop shops" of legal finance because they usually put their own wealth to work, and in some instances also that of affluent relatives, friends, or long-term partners. They operate like small private equity boutiques, regularly updating their partners and,

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sometimes, consulting with them on major portfolio decisions. The "mom-and-pop" financiers focus largely on a local or regional legal community, comprising from one city to several states.

The right tail of the spectrum is populated by different operators: large funds, run by sophisticated asset managers, with AUMs that in some cases exceed the $200 million mark.[111] Heavyweight funders operate nationally and are organized like specialized credit institutions. They invest in a systematic way, relying on formal procedures and "prudential rules."

The AUM of a third-party funder is relevant for the composition of his portfolio. The number of assets in a portfolio is likely to increase somewhat with the portfolio's size.[112] More importantly, the capital available to a funder determines the scale of business he can underwrite. The question here is not whether a funder could afford to spend the money, but whether doing so would not upset the balance of his portfolio. Put differently, the reason why some investments get rejected is not that the sum required is larger than what the funder has left in the tank; but because it is larger than what he can reasonably allocate to a single case. Large, capital-intensive suits can only be bankrolled by funders with enough financial muscle to make enough bets of similar scale.[113] Therefore, the higher a fund's AUM, the larger and more diversified its clientele.

The mode of funding matters as well. Although some pre-settlement, appellate, and post-settlement financiers alike are capable of putting many millions of dollars on a single bet,[114] given the same (and large) amount of money, they would probably end up with different portfolio structures. An average post-settlement funder would aggregate the highest number of legal claims, but his mean per-case investment

111. I derive information on fund sizes from the financial disclosures made by publicly listed funds (Juridica, Burford, IMF Bentham) and, additionally, confidential internal documentation pertaining to three privately held law-firm funders. Of the three, two were large and invested in pre-settlement claims (both reported portfolios worth more than $200 million). The third was a leading post-settlement financier with the AUM of more than $50 million. I corroborated that anecdotal data by triangulating it with statements made by the interviewed insiders, often more open about their peers' money than their own. Finally, some supporting evidence came from observation. For example, one of the smaller fund managers had his office adorned with "trophy" glass stands, memorizing past rounds of capital raising. A caveat is to be made here: AUMs as self-reported by private funders may not be directly comparable, as in some cases they represent the fair value of the portfolio rather than an investment held at cost.

112. My fieldwork data on this topic suggests that the smallest funders (outside of those who opportunistically engage in sporadic transactions) would normally have a number of clients in the "low teens." Large commercial funders would usually have more than 20, but probably less than 40 open positions (for example, Juridica's portfolio at its peak had 25 active investments; Burford has never reported more than 35 assets in their litigation pool). The largest law-firm funds may hold a somewhat larger number of assets, likely more than 50.

113. Several interviewed managers asserted that they were constrained by the supply of capital rather than the demand, and that they could expand quickly if given more cash.

114. Some funders would treat extraordinarily large investment opportunities as special cases. Those would usually be subject to special financial arrangements with shareholders, requiring either an explicit approval or a capital call on investors (mainly hedge funds) with whom the funder has a relationship and who are interested in select, large-scale risks.

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would be the lowest. An appellate funder should be expected to invest in fewer lawsuits of high mean value. And a pre-settlement funder would likely prefer to commit medium-to-high sums and maintain a moderate number of clients.

B. Who's Who in American Litigation Funding

The American market for third-party financing of litigation remains in its nascent stage, and the number of financiers with a meaningful market presence is small. There are probably about twenty providers currently offering business-to-business financing related to legal claims.

The "commercial" funders include two publicly listed companies, Juridica Investments, and Burford Capital, more recently joined by Bentham Capital, the American subsidiary of IMF Bentham, a funder listed in Australia.[115] There are also at least three "private-equity" litigation funding firms: Parabellum Capital,[116] Juris Capital, and the more recent entrants, such as Gerchen Keller Capital,[117] and Lake Whillans Litigation Finance.[118]

The segment of "law-firm" funders has two leaders: Law Finance Group,[119] and Counsel Financial Services. They are followed by Advocate Capital, Amicus Capital Services, and Appeal Funding Partners.

There is also a group of "consumer" funders who in recent years ventured into the territory of business-to-business litigation financing by starting to offer their services to attorneys. Those include LawCash,[120] RD Legal Funding,[121] Case

115. The parent of Bentham Capital LLC is Bentham IMF Ltd., a leading Australian third-party litigation financier listed at the Australian Stock Exchange. In 2014, the funder expanded further, starting a European joint-venture with Elliot Management.

116. Parabellum Capital LLC was spun off by the Credit Suisse group in 2012.

117. With deep ties to top-notch law firms and Wall Street investment banks, Gerchen Keller demonstrates that big money likes silence. Started in 2014, the Chicago-based fund quickly gained prominence, raising more than $1.4 billion in investor commitments. *See* Julie Triedman, *Topping $1 Billion Mark, Big Litigation Funder Gets Bigger*, AM. LAWYER (Jan. 6, 2016), http://www.americanlawyer.com/id=1202746351295/Topping-1-Billion-Mark-Big-Litigation-Funder-Gets-Bigger#ixzz3wynvscKg.

118. The youngest among commercial funding companies, Lake Whillans offers a good anecdote that litigation finance is truly a close-knit community. One of the fund's principals, Boaz Weinstein, was previously the Director of Underwriting at the now-defunct BlackRobe Capital Partners. *See supra* note 71. Another founder, Lee Drucker, worked for both Burford and BlackRobe. *See Our Team,* LAKE WHILLANS, http://lakewhillans.com/our-team (last visited Jan. 10, 2016).

119. Law Finance Group operates under a complex structure. Different entities are engaged in different funding activities and are backed by different investor pools. The group as a whole is hereinafter referred to as Law Finance Group or LFG.

120. LawCash is the flagship brand of Plaintiff Funding Holding Inc. The group includes several different brands, some of which it acquired through mergers or acquisitions as a result of the consolidation in the third-party funding market.

121. RD Legal Funding is another group, and it includes a number of entities, both on- and offshore. The group is hereinafter referred to as RD Legal Funding or RDLF.

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Funding, Peachtree Financial Solutions,[122] Ardec Funding, and American Asset Finance.

Note that the same third party may provide several types of funding. Although funders are often recognized in the market for a distinct expertise, many have diversified away from their original specialty,[123] or evolved.[124]

Table 1 below lists the funders by market segment, and specifies their target clientele and major business models.

Table 1*

122. Peachtree Financial Solutions [hereinafter Peachtree] is a subsidiary of JGWPT Holdings, Inc., after its 2011 merger with the J.G. Wentworth group. The merged entity is controlled by JLL Partners, a private equity firm. *See* JGWPT Holdings Inc., Prospectus 7, 75 (Nov. 8, 2013).

123. For example, Counsel Financial has been primarily a pre-settlement funder, but later started offering post-settlement financing. *See ExpressFee Post-Settlement Funding*, COUNS. FIN., http://attorneylending.com/expressfee (last visited Oct. 14, 2015). LFG has been another market leader in pre-settlement funding, but it is also present in the appellate and post-settlement markets, and even has a separate, niche line focused on trusts and estates. *See Law Finance Group Funding*, LAW FIN., http://www.lawfinance.com/funding.html (last visited Oct. 14, 2015). Peachtree and Case Funding began with post-settlement advances to plaintiffs and later also funded their lawyers.

124. One of the most spectacular examples of an evolving third-party litigation funder is Esquire Bank, a Brooklyn-based, FDIC-insured savings association established in 2006 dedicated to servicing attorneys, primarily on the plaintiff side. The bank appears to be closely affiliated with the founders of LawCash. *See supra* note 120. As of the end of 2013, the bank had about $60 million in outstanding "commercial and industrial loans" to small businesses, about $22 million of which was comprised of loans with outstanding amounts under $1 million. *See* Esquire Bank, Consolidated Reports of Condition and Income for a Bank with Domestic Offices Only—FFIEC 041, 17, 21 (last updated June 5, 2014), https://cdr.ffiec.gov/Public/ViewFacsimileDirect.aspx?ds=call&idType=fdiccert&id=58140&date=12312013. The bank also sources a large part of its deposits from attorneys with whom it has relations and for whom it holds deposits, escrows, and segregated accounts. *See* Letter from Andrew C. Sagliocca, President & Chief Exec. Officer, Esquire Bank, to Shareholders (May 17, 2013), https://www.esquirebank.com/custom/fi/esquirebank/fb/disclosure/Stockholder-Letter-Year-End-2012.pdf. In a way, Esquire Bank can be characterized as a pioneer intermediary facilitating peer-to-peer lending among attorneys.

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Name	Target			Main Lines of Business		
	C	F	I	pre-settlement	appellate	post-settlement
COMMERCIAL FUNDERS						
Juridica Investments	+	+		✔✔	✔	
Burford Capital	+	+		✔✔	✔	✔
Bentham Capital	+	+		✔✔	✔	
Gerchen Keller Capital	+	+		✔✔	✔	
Parabellum Capital	+	+		✔✔	✔	
Lake Whillans	+			✔✔		
Juris Capital	+			✔✔		
LAW-FIRM FUNDERS						
Counsel Financial		+		✔✔		✔
Law Finance Group		+	+	✔✔	✔✔	✔
Advocate Capital		+		✔✔		✔
Amicus Capital Services		+		✔✔	✔	
Appeal Funding Partners		+			✔✔	
CONSUMER FUNDERS						
Peachtree Fin. Solutions		+	+			✔✔
RD Legal Funding		+	+	✔		✔✔
LawCash		+	+	✔		✔✔
Case Funding		+	+	✔		✔✔
American Asset Finance		+	+			✔✔
Rapid Funds		+	+			✔✔
Ardec Funding		+	+			✔✔

* Providers of business-to-business litigation financing identified as having a meaningful presence in law-firm funding market in the United States. Funders are grouped by type ("commercial," "law-firm," and "consumer"), and described in terms of targeted fundee groups ("C"-corporations; "F"-law firms; "I"-individuals) and their primary (✔✔) and secondary (✔) business strategies.[125]

125. The list is not exhaustive. Listed entities were recognized by my contacts, identified in transactional documentation, or disclosed in public records as parties engaged in a meaningful third-party funding business of a given kind. Each listed funder has a website, as do many others who are not on the list. A Google search yields numerous results pointing to such websites (virtually all of them boasting that their owners are market leaders). A listing relying on such Internet claims, without more, is likely to generate a significant number of false-

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Conclusion

Litigation funding is a novel business practice of investing in valuable private claims. It remains unregulated, but rules of law and legal ethics have a significant, if not always intended, impact on how business gets done. Transactions pivot around the represented litigant, her lawyer (either of whom may be funded), and the funder. But there are also other stakeholders: investors whose capital funders manage, and providers of ancillary, often novel, services relevant for legal finance. How those actors interact depends on the market segment and strategies developed there. Financiers may invest early ("pre-settlement"), in midstream (at the "appellate" stage), or late ("post-settlement"). They may have a recourse to all assets of a fundee, a pool of litigation-related claims, or a single claim. Some bets remain passive; in others funders are actively involved, to the point of full control.

It is difficult to find a better example of legal pragmatism than litigation funding. To third-party investors, legal claims are marketable assets, and justice has its price—quite literally. When viewed through their lens, modern civil litigation is more than a forum for redress of private grievances. It is also a clearinghouse for complex financial interests attached to legal claims presented, assessed, and settled through the legal infrastructure. Lawyers who man that judicial machinery become producers of legal goods—adding together and breaking down ingredients of a legal matter until a chunk of justice is churned out.

But such a mercantile approach to law-protected private rights challenges those who occupy traditional places at the production line of justice—judges, attorneys, and policymakers. When claims become business assets with multiple stakeholders, the notion that a civil case is a courtroom duel between a plaintiff and a defendant misses much of what is going on.

Litigation finance is here to stay, in the United States and elsewhere. It deserves a careful and nuanced policy response, defining rights and obligations of various actor groups engaged in the practice of third-party litigation financing based on sound understanding of which each of those actors actually does. A smart regulation is clearly called for. As the first step, however, legislators, lawyers, and judges must recognize the presence of financial stakeholders and their separate interests and motives as a legitimate aspect of litigation.

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positives—for not everyone who claims to fund lawyers actually does. After all, it is much easier to start a website than raise an investment fund.

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