ABSTRACT: Third party litigation finance (TPLF), in which non-parties in litigation give parties money in exchange for a beneficial interest in the outcome of the litigation, has increased rapidly in the United States over the past twenty years. Different markets have emerged involving consumer and corporate plaintiffs, and TPLF has also been adapted for use in mass litigation (class actions and multi-district litigation). As a result, observers and courts have proposed that TPLF be disclosed in litigation in a submission to the court. This paper reviews the arguments for disclosure (including the different ways in which disclosure could occur and the costs and benefits of disclosure). This paper argues that many of the arguments for disclosure are unproven or speculative. It argues that the costs to plaintiffs of disclosure may be high and that the benefits are likely to be low. It concludes that two limited types of disclosure may be justified, notwithstanding its conclusion that broad TPLF disclosure impose unjustified costs on the civil justice system.

I. Introduction

A. Defining Third Party Litigation Finance

Third party litigation finance (TPLF) does not have a single meaning.¹ Most frequently, TPLF is used to refer to financial support of litigation by a stranger in exchange for a share of the proceeds generated by that litigation.² TPLF under this description is identical to the old common

¹ See Victoria A. Shannon, Harmonizing Third-Party Litigation Funding Regulation, 36 CARDOZO L. REV. 861, 863 n.3 (2015) (discussing range of transactions included in definition of TPLF).

² Third party litigation funding is the commercial financing of an individual or portfolio of lawsuits by a person or entity that is not a party to the litigation itself. Although contingency fees and insurance coverage also constitute forms of funding by non-parties, we use the term TPLF in this paper to connote funding provided by firms on a non-recourse basis, in exchange for a share of the settlement or judgment proceeds.

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, 111-12 (2013); see also Miller UK Ltd. v. Caterpillar, Inc., 17 F. Supp. 3d 711, 718 (N.D. Ill. 2014) (TPLF is “where money is advanced to a plaintiff, and the funder takes an agreed upon cut of the winnings. If the plaintiff loses the case, the funder may get nothing.”).
law practice of champerty. However, TPLF may also refer to practices that are related, but not identical to champerty. Financial support of litigation by a stranger on a gratuitous basis, not in exchange for future proceeds and not motivated by a desire for profit, is maintenance. Maintenance, although rare, is a form of TPLF.

Some observers of the TPLF market use the term to refer to transactions between nonlawyers and lawyers where the nonlawyer advances capital to the lawyer in exchange for a future payment based on the lawyer’s receipt of a fee, if and when that occurs. This form of TPLF is neither champerty nor maintenance, since the third party funder is not providing support directly to a party in litigation. Many commentators caution against treating capital advances to lawyers as identical to third party investment in lawsuit through direct payments to litigants. Although the legal and economic circumstances of capital advances to lawyers are a non-standard form of TPLF, they will be covered in this White Paper, although distinguished from standard TPLF, which involves a transaction with a party, not her lawyer.

B. TPLF Markets

TPLF, when it is limited to champerty, is divided in the United States between the commercial and the consumer sectors. In the former, funding is provided to a highly sophisticated litigant, usually a corporation, to help pay for the attorneys and their costs in a commercial dispute. In the latter, funding is provided directly to individuals, most of whom have never engaged previously in litigation. Importantly, consumer TPLF allows money to flow directly to the litigant,

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7 See e.g., Nora Freeman Engstrom, Lawyer Lending: Costs and Consequences, 63 DEPAUL L. REV. 377, 383 (2014) (capital advances to lawyers are “more different than alike” other forms of TPLF); Shannon, Harmonizing Third-Party Litigation, supra note 1 at 863 n.3).

8 For a complete discussion of capital advances to lawyers, see Anthony J. Sebok, Selling Unearned Attorneys’ Fees 2018 ILLINOIS L. REV. __.


10 Ibid at 13.
providing an important source of financial support during the pendency of litigation.\textsuperscript{11} Funding contracts differ in type between the two sectors. Commercial TPLF usually pays the funder a percentage of the litigation proceeds upon resolution of the litigation.\textsuperscript{12} In contrast, in consumer TPLF the funder receives a payment based on monthly or semi-annual interest charges determined by the length of time to the resolution of the litigation.\textsuperscript{13}

When TPLF is extended to include direct funding of lawyers, the form of the transactions are hard to generalize, since there is very little publicly available information about third party funding of lawyers. The market seems to be divided into three types of transactions. First, there are transactions between funders who advance capital in exchange for a security interest in the unearned fee of a single case or a small number of identifiable cases.\textsuperscript{14} Second, there are transactions between larger commercial funders and law firms in which capital advances are secured by “portfolios” of cases.\textsuperscript{15} Third, there have been reports of TPLF provided to a law firm seeking to be appointed lead counsel in a class action.\textsuperscript{16}

\begin{itemize}
\item \textsuperscript{11} Id. at 9.
\item \textsuperscript{12} In commercial litigation finance contract “the financier provides immediate capital to prosecute the case in exchange for a percentage of the future recovery.” Joanna M. Shepherd & Judd E. Stone II, Economic Conundrums in Search of a Solution: The Functions of Third-Party Litigation Finance, 47 ARIZ. ST. L.J. 919, 937 (2015). But there is no “one size fits all” commercial litigation finance contract. Commercial funding is diverse and includes many different types of products. See, e.g. Maya Steinitz, The Litigation Finance Contract, 54 WM. & MARY L. REV. 455 (2012) and see Shepherd & Stone, Economic Conundrums in Search of a Solution at 941-42 (on the use of “first money out” and “waterfall” payment structures).
\item \textsuperscript{13} See Garber, supra note 9 at 9.
\item \textsuperscript{14} The following courts have upheld the assignment of a security interest in an unearned contingent fee in exchange for a capital advance. Hamilton Capital VII, LLC v. Khorrami, LLP, 2015 NY Slip Op 51199(U), 48 Misc. 3d 1223(A), 22 N.Y.S.3d 137 (Sup. Ct.); Lawsuit Funding, LLC v. Lessoff, 2013 WL 6409971 (NY Sup. Crt. 2013); Kelly, Grossman & Flanagan, LLP v Quick Cash, Inc., 35 Misc. 3d 1205(A) (N.Y. Sup. Ct. 2012); PNC Bank v. Berg, No. 94C-09-208-WTQ, 1997 Del. Super. LEXIS 19, at *27 (Super. Ct. Jan. 31, 1997). In Lessoff, for example, the agreement “called for Plaintiffs to receive a portion of the contingent legal fee that Defendants were expected to receive if five specifically named lawsuits were adjudicated in favor of Defendants’ clients.” Lessoff at *2. In addition, in Counsel Fin. Servs. v. Leibowitz, 2013 Tex. App. LEXIS 9252 (13th Dist. Ct. App.), the court recognized contract rights in an unearned contingent fee defined by the application of an interest rate to a fixed sum.
\end{itemize}
II. Arguments for Disclosure

A. Introduction

It is crucial to distinguish at the outset the difference between proposals for disclosure of TPLF, in their various forms, and other proposals concerning the regulation or elimination of TPLF. Disclosure of TPLF relates to mandatory requirements concerning information about TPLF. The range of other proposals concerning the regulation and elimination of TPLF is vast, and beyond the scope of this White Paper. It should be noted, in passing, that some states prohibit all TPLF and some states have imposed limitations on only consumer TPLF, either as a matter of judicial interpretation or legislative enactment. Some of the same groups that have called for disclosure have also called for other forms of regulation (or elimination) of TPLF.

B. Arguments for Disclosure in Commercial TPLF

Arguments for disclosure of TPLF have arisen in two waves. In the first wave, defendants have attempted to obtain documents related to TPLF from adverse parties in litigation. Typical of such a request was that of the defendant in Miller UK Ltd. v. Caterpillar, Inc., who asked for “the actual contract with Miller’s [the plaintiff] funder and those documents provided by Miller to it and any other third party lender from which Miller sought funding for this case.” The reasons for requesting the documents was that they would be relevant to helping the defendant determine whether it had a defense of champerty under state law, who was the real party in interest under Rule 17(a) of the Federal Rules of Civil Procedure (“FRCP”), and that the documents contained material relevant to the underlying issue of liability and damages. Most courts that have been asked to enforce discovery motions to disclose TPLF-related documents have rejected the requests on the ground that the documents contain attorney work product, and the conditions for waiver of


17 F. Supp. 3d 711, 713 (N.D. Ill. 2014).

18 Ibid. at 719 and 739 – 40.
work product have not been satisfied per FRCP Rule 26(b)(3)(B). On at least one occasion a court has rejected discovery of TPLF-related documents on the ground that the requested documents were not relevant to the underlying litigation.

The second wave has come in the form of proposals to amend state and federal law. Typical of these proposals is the following, which was proposed by the U.S. Chamber Institute for Legal Reform to FRCP 26(a)(1)(A) in 2017:

a party must, without awaiting a discovery request, provide to the other parties . . . for inspection and copying as under Rule 34, any agreement under which any person, other than an attorney permitted to charge a contingent fee representing a party, has a right to receive compensation that is contingent on, and sourced from, any proceeds of the civil action, by settlement, judgment or otherwise.

This proposal is identical to one which the U.S. Chamber proposed in 2014 and 2016. A nearly identical proposal was recently passed in Wisconsin:

Third party agreements. Except as otherwise stipulated or ordered by the court, a party shall, without awaiting a discovery request, provide to the other parties any agreement under which any person, other than an attorney permitted to charge a contingent fee representing a party, has a right to receive compensation that is contingent on and sourced from any proceeds of the civil action, by settlement, judgment, or otherwise.

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23 See *Miller*, 17 F. Supp. 3d at 723.


25 See Report to the Standing Committee of the Advisory Committee on Civil Rules, December 6, 2017 at 247 (“Standing Committee Report”).

26 2017 Assembly Bill 773 (“SECTION 12. 804.01 (2) (bg) is created to read”). The bill was signed into law on April 2, 2018.
The proposal to amend Rule 26 has been explained in materials from various tort reform organizations which are publicly available. The letters from the U.S. Chamber and the Request for Rulemaking to the Advisory Committee on Civil Rules from Lawyers for Civil Justice raise multiple concerns about TPLF.27 These sources suggest that disclosure would protect “the integrity of the adversarial process”28 in the following ways:

1. Expose violations of laws against champerty, where they exist;29  
2. Expose violations of the prohibition against fee-splitting between lawyers and non-lawyers;30  
3. Expose agreements which create impermissible conflicts of interest between lawyers, funders and clients;31  
4. Expose conflicts of interests between judges and funders;32  
5. Expose efforts by funders to control litigation;33  
6. Expose contract terms that might “undermine” settlement;34  
7. Allow judges to weigh the resources available to parties to determine discovery;35  
8. Allow judges to know who the real party in interest is, if sanctions are imposed;36  
9. Allow judges to know whether a third party in addition to plaintiffs are interested in the result of a class or mass action;37  
10. Allow “parity of financial disclosure” similar to Rule 26’s requirement that parties (usually defendants) disclose the existence and terms of liability insurance.38  
11. Allow the public to know whether a third party with a non-economic, social or political motive is using a party in litigation; in other words, to make it harder for someone like Peter Thiel to fund a lawsuit against a defendant like Gawker Media.39

28 See Chamber Letter at 11.  
29 Ibid.  
30 Id. at 13.  
31 Id. at 14.  
32 Id. at 15.  
33 Id. at 16.  
34 Id. at 18.  
35 Id. at 19.  
36 Id. at 19.  
37 Id. at 20.  
38 Id. at 22. Many of these points are repeated in the Request for Rulemaking at 9 – 10.  
39 See Andrew Ross Sorkin, Peter Thiel Is Said to Bankroll Hulk Hogan’s Suit Against Gawker, NEW YORK TIMES, May 25, 2016 at B3. According to sources present at the debate of the Wisconsin bill, the “Peter Thiel” problem was raised by proponents of the bill to convince some skeptics. This is based on the author’s personal knowledge.
As the Standing Committee of the Advisory Committee on Civil Rules noted in a report, some of the putative justifications for disclosure are moot if the problem that they are supposed to cure does not exist in practice, such as the problem that TPLF allows funders to control litigation (something funders deny) or undermine settlement (again, something funders deny).\textsuperscript{40} Other justifications may be possible, such as conflict of interests between judges and funders where a judge owns shares in a commercial funder, or the risk that a TPLF contract is in violation of state law, but then there is a question of costs versus benefits – whether a rule that requires compulsory disclosure is worth the costs that it would impose.\textsuperscript{41}

C. Arguments for Disclosure in Consumer TPLF

The arguments reviewed above for disclosure have been raised primarily by critics of commercial TPLF and have received responses from primarily commercial funders such as Burford and Bentham. Consumer TPLF would be affected by the disclosure rules proposed for Rule 26, and will be affected by the new disclosure rule adopted in Wisconsin, but the consumer TPLF companies have not expressed much of an opinion about disclosure. This may be for a number of reasons, the most significant that consumer TPLF firms are much more concerned with other changes to the law of TPLF that are separate from proposals concerning disclosure. Consumer TPLF companies are concerned with changes to the law that would treat TPLF contracts with consumers as loans or as advances subject to limits similar to those imposed by usury law or other consumer credit laws.\textsuperscript{42} The automatic disclosure requirement adopted by Wisconsin will apply to a $2500 consumer TPLF contract as well as a $2 million commercial TPLF contract, but it seems that this extra burden was not of great concern to the consumer TPLF companies. Their main concern was to remove from the bill language which would have defined TPLF as “lending,” which might have brought their contracts within Wisconsin’s usury law.\textsuperscript{43} They were successful.\textsuperscript{44} Another reason that consumer TPLF firms may not be concerned with disclosure proposals is that, the existence of TPLF may be of little or no interest to the adverse party, since TPLF contracts are

\textsuperscript{40} Standing Committee Report at 248 (“Third-party funders meet [some of] these arguments by direct denial. None of them . . . are true.”).

\textsuperscript{41} Ibid at 250.


based on templates and their terms reveal nothing about the underlying case or any lawyer’s work product.\textsuperscript{45}

Disclosure in the context of consumer TPLF can mean more than allowing adverse parties to know about the existence of a funding agreement and the content of that agreement. It can mean regulatory requirements that funders provide information to the consumer. It can also mean regulatory requirements that funders provide information to a public agency (either state or federal).

On February 17, 2005, the Attorney General of the State of New York and nine New York based consumer TPLF firms entered into an "Assurance of Discontinuance" agreement that resulted from negotiations between the Attorney General and the LFCs.\textsuperscript{46} The main purpose of the N.Y. Agreement was to put into place certain disclosure requirements that TPLF firms would have to provide to consumers in the State of New York. The N.Y. Agreement imposed nine requirements, modeled after standardized credit card and mortgage applications. The key requirements were a clear statement of the financial terms of the agreement, including a statement of the (a) the total amount being advanced; (b) an itemization of one time fees broken out item by item (e.g., application, processing, attorney review, broker, etc.); (c) the annual percentage interest rate charged and how often interest compounds; and (d) the total amount the borrower will repay broken out by six month intervals and carried forward to thirty-six months, including all fees and the minimum payment amount, as well as a five business day period to cancel the contract without suffering a penalty. It does not impose an upper limit on how much the funder can charge in interest, fees, or other costs.

Since 2005, the two major consumer TPLF trade organizations have adopted voluntarily codes of conduct that parallel the N.Y. Agreement.\textsuperscript{47} Five states, Maine, Nebraska, Ohio, Oklahoma, and Vermont, have adopted disclosure laws that, with some variation, endeavor to provide consumers protection through forcing TPLF firms to provide information similar to that disclosed under the N.Y. Agreement.\textsuperscript{48} Indiana has adopted a law with disclosure requirements similar to

\begin{footnotesize}
\begin{enumerate}
    \item Further, given that consumer TPLF concerns cases that rarely go to trial (or even progress into significant discovery) it may be that, to the extent that funders are concerned that judges may respond to the existence of funding, the risk of judicial notice of consumer TPLF is extremely low.
\end{enumerate}
\end{footnotesize}
those of the N.Y. Agreement, but since it also has a cap on the price of consumer TPLF, the legislation is not seen primarily as a disclosure law, and it was only grudgingly endorsed by one of the two TPLF trade organizations.\footnote{Indiana Code 24-4.5-3-202 (effective July 1, 2016) (maximum rate of 36%) and see Victor Li, Indiana and Vermont Regulate Consumer Litigation Funding, ABA JOURNAL, July 7, 2016 at http://www.abajournal.com/news/article/indiana_and_vermont_regulate_consumer_litigation_funding (on ARC’s views of Indiana TPLF law).}

In addition to the forcing a clear statement of existing contract terms, which is what the N.Y. Agreement does, disclosure could also include additional information not contained in the contract, and it could include disclosure to third parties other than the consumer or the defendant, such as a state or federal agency tasked with collecting information. Up to now, proposals under the heading of “disclosure,” which have been promoted mostly by consumer TPLF trade groups, have focused on making existing contract terms as clear as possible. For example, the proposed legislation currently favored by ALFA in New York would require “an itemization of one-time charges; the maximum total amount to be assigned by the consumer to the company, including the funded amount and all charges; and a payment schedule to include the funded amount and charges, listing all dates and the amount due” at the end of six month periods.\footnote{See Senate Bill S8860 (“Third Party Litigation Financing”), introduced by Sen. Razenkofer, May 29, 2018 at §899-GGG (“Disclosures”). The proposed legislation would also require consumer TPLF firms to report the “number of consumer litigation fundings” by each firm; a “summation of funded amounts”; the “annual percentage charged to each consumer where repayment was made” and these figures would be made available to the public. Ibid at 899-LLL (“Reporting”).}

Recent empirical research into the behavior of the consumer TPLF suggests that, while the price of consumer TPLF is not as high as its critics have suggested, the market is extremely opaque and consumer may not be receiving the same final price for the sale of their asset.\footnote{See Ronen Avraham & Anthony J. Sebok, An Empirical Investigation of Third Party Consumer Litigation Funding, 104 CORNELL L. REV. __ (2018) and Ronen Avraham & Anthony J. Sebok, Americans Should Have The Proper Protections When Bringing Lawsuits, THE HILL, March 29, 2018 at http://thehill.com/opinion/judiciary/380891-americans-should-have-the-proper-protections-when-bringing-lawsuits.} Disclosure of whether consumer TPLF companies have adjusted the final price charged to the consumer after the resolution of the consumer’s lawsuit, and the actual average price charged to consumers, is something that consumers and regulators may benefit from knowing. Mandatory disclosure of this data is another form of disclosure, different from either the disclosure to adverse parties urged in the context of commercial TPLF and disclosure of contract terms which has been the primary focus of consumer TPLF trade groups.

\section*{D. Arguments for Disclosure of Law Firm Financing}

As noted above, proponents of disclosure of commercial TPLF argue that it would help enforce ethical prohibitions on fee-splitting.\footnote{See, e.g. Chamber Letter at 13.} This justification for disclosure has been challenged by some academic experts in legal ethics, who argue that it is highly unusual for the federal rules
of procedure to be used to promote the enforcement of rules of professional responsibility, which are clearly the province of the states and (as in the case of so-called fee-splitting) may not mean the same thing in all states.  

Proponents of disclosure have additional arguments that do not depend on using federal rules of civil procedure to support or reinforce state law. They argue that in the context of mass and class federal actions, disclosure of third party funding of law firms promotes the ends of the federal rules under which the lawyers operate.

In the context of class action, proponents of disclosure have argued that the existence of TPLF is necessary for a court to evaluate the adequacy of class counsel under FRCP 23(a)(4)’s adequacy-of-representation prerequisite. The argument has found support in Gbarabe v. Chevron Corp., where a lawyer seeking appointment as lead counsel was required to disclose the terms of a commercial TPLF agreement. Furthermore, the same federal district court in which Gbarabe was decided has adopted a local rule requiring the disclosure of TPLF in cases brought under FRCP Rule 23. At least one other federal district courts is considering a similar step. The motivation behind the disclosure rule adopted by the Northern District of California is not public, and there is reason to believe that the judges who adopted the rule were motivated by concerns beyond law firm finance in class actions, or only law firm finance. On May 10, a bill was introduced in the United States Senate which would amend the portion of the United States Code pertaining to class actions to require disclosure of TPLF. The bill’s disclosure requirements are similar to those required by the Northern District of California. In a press release, the senators sponsoring the bill

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54 See, e.g., Chamber Letter at 21.
56 See Standing Order for all Judges of the Northern District of California, Contents of Joint Case Management Statement, § 19 (Jan. 2017), requiring that “in any proposed class, collective, or representative action, the required disclosure includes any person or entity that is funding the prosecution of any claim or counterclaim.”
57 See Ben Hancock, Bentham Hires Yetter Coleman Partner as It Expands to Texas, TEXAS LAWYER, Feb. 21, 2017, https://www.law.com/texaslawyer/almID/1202779591965/Bentham-Hires-Yetter-Coleman-Partner-as-It-Expands-to-Texas/ (“Ron Clark, chief judge of the Eastern District of Texas, told Texas Lawyer that jurists in his division may follow the Northern District of California’s lead and consider similar measures.”)
58 See Ben Hancock, Northern District, First in Nation, Mandates Disclosure of Third-Party Funding in Class Actions, THE RECORDER, January 23, 2018, https://www.law.com/therecorder/almID/1202777487488/Northern-District-First-in-Nation-Mandates-Disclosure-of-ThirdParty-Funding-in-Class-Actions (“The court's Civil Rules Committee, chaired by Judge Richard Seeborg, had proposed a broader rule that would have required the automatic disclosure of funding agreements in any matter before the court” but it was narrowed.).
said that TPLF in class actions may create a risk of “conflicts of interest” which could be addressed by disclosure.\textsuperscript{60}

Finally, disclosure in litigation connected multi-district litigation, or MDLs, has been urged.\textsuperscript{61} The policy concern behind disclosure in connection with MDLs is – according to its proponents – the risk that TPLF companies are financing so-called “lead generators” or “aggregators.”\textsuperscript{62} The facts behind this concern are hard to evaluate, since the practices lumped under the terms “lead generator” or “aggregator” are vague and involve activities that may be performed by lawyers and nonlawyers.\textsuperscript{63} In general, these third parties help lawyer seeking to participate in MDLs of other mass actions find clients.\textsuperscript{64} The connection between TPLF and disclosure is that if defendants and courts in MDLs can learn about the interest third parties have in lead generation, the risk of frivolous and fraudulent claiming will be reduced.\textsuperscript{65} For this reason, the Lawyers for Civil Justice have, in addition to supporting the amendment to FRCP 26 proposed by the Institute for Legal Reform, proposed amending Rule 26 so that “any third-party claim aggregator, lead generator, or related business or individual, who assisted in any way in identifying any potential plaintiff(s)” would be disclosed.\textsuperscript{66} The one fact that is missing from the policy arguments for disclosure of TPLF financing in connection with lead generation in MDLs (or any litigation, for that matter) is that the degree to which commercial or consumer TPLF firms finance companies (or lawyers) who specialize in identifying plaintiffs for mass tort cases.


\textsuperscript{61} See Rules for Rulemaking at 10 - 11.

\textsuperscript{62} Ibid.


\textsuperscript{64} See Jason Rathod & Sandeep Vaheesan, The Arc and Architecture of Private Enforcement Regimes in the United States and Europe: A View Across the Atlantic, 14 U.N.H.L. REV. 303, 360 (2016) (“[A]ttorneys litigating these cases assemble large inventories, usually with the assistance of a cottage industry of lead generation and referral firms.”).

\textsuperscript{65} See Rule for Rulemaking at 11 – 12.

\textsuperscript{66} See \textit{ibid} at 12:

In order to provide transparency to courts and parties, the Committee should amend Rule 26(a)(1)(A)(i) to include the following required disclosure:

The name and, if known, the address and telephone number of each individual likely to have discoverable information...and if relevant, a disclosure of any third-party claim aggregator, lead generator, or related business or individual, who assisted in any way in identifying any potential plaintiff(s), and if relevant, the identification of any plaintiff that was recommended, referred, or otherwise directed to plaintiff’s counsel based on a recommendation, referral, or other information gathered from such a third party claim aggregator, lead generator, or related business or individual.
Despite the very tenuous connection between MDL lead generation and TPLF firms, the Advisory Committee on Civil Rules chose to continue to consider amendments to FRCP 26 in the context of MDLs. Rather than endorse the disclosure recommendation urged by groups like the Institute for Civil Justice, the committee asked the Subcommittee on MDLs to gather more information about TPLF. It is not clear why the question of disclosure of TPLF was given to the Subcommittee on MDLs. It is also not clear that the committee views itself as limited in future discussions over FRCP 26 to disclosure relating only to MDLs (or class actions). The only thing that is clear is that the Subcommittee on MDLs is currently the institutional focal point of any future efforts to adopt new disclosure requirements on TPLF in the federal rules.

The Litigation Funding Transparency Act of 2018, discussed above, would also require automatic disclosure of any agreement which provides for payment to a commercial third party contingent upon proceeds being generated in a case within the jurisdiction of 28 U.S. Code § 1407, the federal law governing multidistrict litigation. The policy justification for extending the scope of disclosure beyond class actions to MDLs in the Act is not clearly stated by its sponsors, but supporters of the Act have suggested that TPLF in MDLs “allows hedge funds to . . . charge

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68 See March 2018 Report of the Standing Committee to the Chief Justice:

The advisory committee has received a suggestion to add a new Rule 26(a)(1)(A)(v) that would require automatic disclosure of any agreement under which any person, other than an attorney permitted to charge a contingent fee representing a party, has a right to receive compensation that is contingent on, and sourced from, any proceeds of the civil action, by settlement, judgment or otherwise. . . . The committee referred the issue to the MDL subcommittee, since one of the MDL proposals discussed above explicitly calls for disclosure of third party financing agreements. Additionally, such funding agreements are often used in MDL proceedings. The subcommittee will study the issue in an effort to determine whether it is something that should be pursued.

69 At least one member of the Advisory Committee held the view that TPLF is overrepresented in MDLs. See Draft Minutes, Civil Rules Committee, November 7, 2017 in Civil Rules Advisory Committee Agenda Book (April 2018) at lines 692 – 93 (“A judge suggested that third-party funding seems to be an issue primarily in patent litigation and in MDL proceedings.”).

70 See Standing Committee Report at 250 (emphasis added):

The Committee concluded that these questions can be delegated, at least initially, to the Subcommittee appointed to develop information about the MDL proposals. One of the MDL proposals explicitly incorporates the proposal for disclosure of third-party financing agreements. There is reason to believe that MDL litigation is one of the prominent occasions for third-party funding. This Subcommittee’s work will prepare the way for a determination whether third-party financing disclosure should be pursued.

71 See The Litigation Funding Transparency Act of 2018, section 3.
sky-interest rates — sometimes up to 200 percent — and leave plaintiffs [in MDLs] with settlements of just pennies on the dollar.”72 This is not an argument for disclosure in MDLs per se, as opposed to disclosure in any federal case (which is what the proponents of changes in Rule 26 have recommended) and it is not clear how disclosure would address the evil of high costs of litigation financing to individual plaintiffs, since a federal judge has no authority to determine compensation for individuals in an MDL, although they can monitor the allocation of a common benefit fees where where is an agreement by all parties to settle while a court retains jurisdiction under 28 U.S. Code § 1407.73

III. Cost and Benefits of Disclosure

A. Introduction

Before discussing the costs and benefits of disclosure of TPLF, it must be noted that there is little empirical data upon which to base an evaluation. As mentioned above, the only law or court rules specifically intended to require disclosure of TPLF to the court and an adverse party are the recently enacted Wisconsin law and the local rule adopted by the Northern District of California.

Other local rules that require the disclosure of a party interested in the outcome of litigation, such as Federal Rule of Appellate Procedure 26.1 and Federal Civil Rule 7.1 which concerns corporate disclosure statements, have always existed, but only recently have commentator suggested that they should be interpreted to cover TPLF. The Advisory Committee reviewed existing local rules of federal circuit and district courts and concluded that some of these courts have versions of Rules 26.1 and 7.1 which require disclosure of funding, although none of them were drafted explicitly with that purpose and it is not clear whether these rules have been interpreted until now to require disclosure of TPLF.74 The committee concluded that six federal appellate courts had local rules that extended Rule 26.1 in some way that might require disclosure of the existence of TPLF, such as the local rule in the Eleventh Circuit, which would require disclosure of must contain a complete list of all “persons, associations of persons, firms, partnerships, or corporations that have an interest in the outcome of the particular case or appeal.”75 The same memorandum also noted that, while no other district court “has (yet) followed the Northern District of California’s lead to

74 See Memorandum from Patrick A. Tighe, Rules Law Clerk: Survey of Federal and State Disclosure Rules Regarding Litigation Funding, February 7, 2018 (hereafter “Survey of Disclosure Rules”). Appellate Rule 26.1 provides that “[a]ny nongovernmental party to a proceeding in a court of appeals must file a statement that identifies any parent corporation and any publicly held corporation that owns 10% or more of its stock or states that there is no such corporation.”
identify expressly class action lawsuits as a civil action in which the disclosure of litigation funders is required. . . 23 other district courts require that parties identify litigation funders in any civil action under local rules related to Federal Rule of Civil Procedure 7.1. These district courts, like the circuit courts, have local rules that extend Rule 7.1 and require disclosure of any person or entity (other than the parties to the case) that has a “financial interest in the outcome of the proceeding.” According to the memorandum, the “plain language of these local rules encompasses litigation funders because a litigation funder will receive proceeds from the settlement or judgment if the contracting party prevails,” but although some might require a description of the “nature of litigation funder’s financial interest,” none require disclosure of the litigation finance agreement itself, something the proposed amendment to Rule 26 would require.

As the memorandum notes, the stated justification for the disclosure requirements in the circuit courts “is to help judges assess recusal and disqualification.” The disclosure requirements in the local rules in the district courts, similarly, are intended “to assist judges with assessing possible recusal or disqualification.” The memorandum notes that commercial TPLF companies have not, up to now, considered the disclosure rules discussed in the memorandum to require disclosure of TPLF, and the memorandum cites only one recent episode where TPLF was revealed as a result of court-ordered compliance with a version of Rule 7.1. Further, although it would have been outside of the scope, the memorandum does not discuss how likely disclosure under the rules it reviewed would lead to recusal, since the memorandum does not purport to speculate about the likelihood that judges have relations with TPLF companies that would require recusal under current standards of judicial conduct.

While it is possible that the recent explosion of proposals for disclosure targeted at TPLF is intended to address a dramatic increase in the risk of conflict of interest that existing rules of court are inadequate to prevent, it is likely that the proponents of the new proposals have other ends in mind. As the next section will illustrate, the cost of complying with the proposed disclosure rules may increase depending on their application by the courts. The possibility cannot be ignored that for many of the proponents of the new disclosure rules, uncertainty and excess costs of compliance is a feature, not a bug in the system they wish to create. That is, it may be the case that the goal is to adopt rules whose stated benefits are admittedly rarely realized, but whose real benefit is that they make every TPLF transaction more costly.

76 Survey of Disclosure Rules at 4. FRCP 7.1 provides in relevant part that any “nongovernmental corporate party must file 2 copies of a disclosure statement that: (1) identifies any parent corporation and any publicly held corporation owning 10% or more of its stock; or states that there is no such corporation.”


78 Ibid.

79 Id. at 2.

80 Id. at 5.

81 Id. at 5 – 6 (“compliance with these local rules is difficult to ascertain”, and see Notice of Interested Parties, Realtime Adaptive Streaming LLC v. Hulu, LLC, No. 2:17-cv-07611-SJO-FFM, Dkt. No. 18 (C.D. Cal. Oct. 24, 2017)).
B. Costs of Disclosure

The costs of disclosure can be discussed in only the most general and speculative terms. Obviously, to the extent that some disclosure of TPLF is already required by existing law, it might be observed that the costs seem to be law and manageable, since TPLF is growing and, except for a few disputes over waiver of privilege, the cost of enforcing the current disclosure regime seem relatively low. But the relevant question is whether proposals for additional disclosure, either through the amendment of federal and state laws and local rules, will impose additional costs, and what those costs will be.

1. Direct Economic Costs

It is likely that mandatory disclosure rules will add economic costs the parties in litigation. Parties receiving TPLF will have to take steps to comply with mandatory rules. It is possible that the direct financial costs will be low for consumer TPLF. For example, it may be that one reason that consumer TPLF trade groups did not oppose the recent Wisconsin disclosure law in its final form is that they thought that it would be easy for lawyers to comply with the mandatory disclosure requirement by creating a standard document which would be triggered by a simple review of a client’s file, automatically filled out by software, and filed electronically.

The direct financial costs in the context of commercial TPLF may be greater. The proposed changes to Rule 26 will create a rule which, at least initially, require human judgment in its application. Needless to say, courts in multiple federal circuits and districts will have to interpret the rule, and that will take time to resolve contradictory judicial interpretations. There is no settled understanding of what sort of beneficial interest falls under the phrase “any person . . . [who] has a right to receive compensation contingent on, and sourced from, any proceeds of [a] civil action.”

If the proposed disclosure rules are given their broadest possible application, then the direct financial consequences of reporting may be borne by parties who are not TPLF firms, and are far outside the scope of the policy concerns reviewed above that have motivated the proposed changes. To take a very real example the recently adopted Wisconsin legislation, on its face, would require any person with a contingent right to proceeds to disclose the underlying agreement, including an insurance subrogatee, or a claimant who took a bank loan with the litigation claim as security, or a personal loan among family members, or even a deferred healthcare fee to be paid with the proceeds of a personal injury lawsuit. Regardless of whether these affected parties have any legal or

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82 This is taken from the amendment to Rule 26 proposed by the Institute for Legal Reform, supra note 24.

83 District courts vary in the type of financial interest that parties must disclose. Some require identifying any entity with “a financial interest” whereas others require disclosing only those entities with a “direct financial interest” or a “substantial financial interest.

tactical reason to object to disclosure under these conditions, they will have to bear the cost of compliance.

2. Indirect Economic Costs

The indirect of economic costs of adding new disclosure requirements are very hard to measure. Any added cost to litigation reduces access to justice; this well understood principle that motivates advocates and opponents of so-called tort reform, which is designed, in part, to make it more expensive for parties and their lawyers to bring lawsuits. The direct costs of disclosure were canvassed in the previous section. The indirect costs include (a) increases in the cost of capital, for both parties and plaintiff’s attorneys (if they have to substitute TPLF with advances) and (b) additional litigation expenses generated by pre-trial motion practice – specifically additional discovery requests – prompted by disclosure. Finally, it is possible that the true motivation behind many disclosure proposals is not only to increase direct and indirect costs of litigation, but to affect public opinion about the value and desirability of TPLF. One consequence of disclosure is the possibility of public access to the details of TPLF agreements. There may be a hope that, although most TPLF agreements might be of no interest to the press or the public at large, some agreements might contain terms or reflect motivations that might cast the whole TPLF sector in a bad light.

3. Comparison With Other Disclosure Rules

It is very difficult to draw any conclusions about the direct economic costs of expanding disclosure of TPLF by comparing it to other disclosure laws and rules unconnected to TPLF. As mentioned above, the disclosure regime imposed by Federal Rule of Appellate Procedure 26.1 and Federal Civil Rule 7.1, which have, until now, been intended to help courts avoid conflicts of interest with the parties before them, seem to offer little useful guidance. The only other disclosure rule that might have relevance concerns the mandatory initial disclosure of liability insurance coverage under Rule 26(a)(1)(A)(iv). In 1970, the Committee amended Rule 26(b)(2) to require disclosure of a defendant’s insurance coverage because it felt that “[d]isclosure of insurance coverage will enable counsel for both sides to make the same realistic appraisal of the case, so that settlement

See, e.g., STEPHEN DANIELS & JOANNE MARTIN, TORT REFORM, PLAINTIFFS' LAWYERS, AND ACCESS TO JUSTICE (2015).

Additional discovery costs are one reason that commercial TPLF firms opposed the Wisconsin disclosure legislation. See Ben Hancock, Litigation Funding Deals Must Be Disclosed Under Groundbreaking Wisconsin Law, NATIONAL LAW JOURNAL, April 04, 2018 at https://www.law.com/2018/04/04/wisconsin-litigation-funding (“This provision in the amended statute will, in all likelihood, increase the number of discovery disputes and thus the cost of litigation for both plaintiffs and defendants,’ Allison Chock, the chief investment officer for Bentham IMF, said in an email.”).

While TPLF may be legal, it may also offend public opinion when used for certain ends. This may explain why, for example, Peter Thiel took every effort to conceal his TPLF arrangement in the litigation against Gawker by “Hulk” Hogan. See Ryan Mac, Behind Peter Thiel's Plan To Destroy Gawker, FORBES, June 7, 2016 at https://www.forbes.com/sites/ryanmac/2016/06/07/behind-peter-thiel-plan-to-destroy-gawker/#5876242f30f4.
and litigation strategy are based on knowledge and not speculation.” Amendments to Rule 26 were adopted in order to help parties to make choices about conducting litigation and to allow both sides to have (as much as possible) the same information about resources available for settlement.  

Leaving aside whether the same policy goals would be served by changing Rule 26 to require disclosure of TPLF as are served by requiring disclosure of liability insurance, a separate question can be asked about the burden imposed by the two disclosure regimes. The mandatory disclosure requirement of liability insurance in Rule 26 is much narrower in scope than the proposal to require mandatory disclosure of TPLF under discussion. As the Advisory Committee on Civil Rules noted:

[D]isclosure is carefully limited to an agreement with “an insurance business.” Other forms of indemnification agreements are not covered. Nor is discovery generally allowed into a defendant’s financial position, even though both indemnification agreements and overall resources may have impacts similar to, or even exceeding, the impact of liability insurance.

The proposed amendment to Rule 26 would extend to “any agreement under which any person, other than an attorney permitted to charge a contingent fee representing a party, has a right to receive compensation that is contingent on, and sourced from, any proceeds of the civil action, by settlement, judgment or otherwise,” and thus would extend to a far larger universe of materials.

The significance of the more limited obligation in Rule 26’s liability insurance disclosure requirement can be seen in the court’s rejection of efforts by parties to go beyond the strict disclosure requirements of the rule to obtain documents related to the amount of a party’s right to coverage. Courts have refused plaintiffs access under Rule 26 to an insurer’s reservation of rights letter connected to a liability policy or an accounting of how much of the policy limits in a policy had been used for legal fees before an insured had assumed the cost of its own representation and secured new counsel. The plain meaning of the Chamber’s proposal—to require mandatory disclosure of “any agreement” involving litigation finance—would allow a defendant to obtain information about a plaintiff’s litigation posture that courts prohibit plaintiffs from securing under the insurance disclosure requirements supporters of expanded disclosure for TPLF. Regardless of whether the additional burden is worth it, it must be admitted that the scope of the obligation will be greater for plaintiffs than defendants.

87 Fed. R. Civ. P. 26(b)(2) advisory committee’s note to 1970 amendment.
88 Standing Committee Report at 248.
89 Ibid.
90 This is true about the Wisconsin law as well.
4. Costs to Lawyers

In addition to the direct and indirect costs of compliance detailed above, which assume that legal resources will have to be dedicated towards complying with, and interpreting, the obligations that TPLF disclosure rules would impose, there is an additional cost that is borne only by lawyers. Compliance assumes competent legal advice, which, of course, is the basic obligation of all lawyers. Unless a lawyer chooses to limit her scope of representation and explicitly refuse to advise a client on compliance with new TPLF disclosure requirements, she will have to advise a client on compliance, and probably assist the client as well, by gathering materials and filing the relevant forms. None of this represents unusual legal work (as is evidenced by the fact that that certain statements relating to liability insurance coverage is presumably compiled by lawyers under FRCP Rule 26(a)(1)(A)(iv) for defendants) but it represents an expansion of a lawyer’s exposure to both discipline and malpractice liability. Failure by a lawyer to reasonably advise a client on new mandatory disclosure requirements may result in injury to the client, and therefore civil liability. Failure by a lawyer to disclose any documents within the scope of a mandatory TPLF disclosure rule (or to amend after the fact a failure of a client to disclose) would open the lawyer up to discipline under Rule 3.3(a)(1). Lawyers have already been sued (albeit unsuccessfully) by clients who have been unhappy with their advice with regard to a TPLF contract. Clearly, by expanding the exposure of lawyers to liability and discipline, additional costs (of care, self-insurance, and malpractice insurance) will be imposed on lawyers who have clients who seek TPLF.

B. Benefits of Disclosure

Like the costs of disclosure, the benefits are also speculative and hard to predict (or measure). The most commonly cited benefit is that by requiring TPLF to be disclosed at an early stage in litigation, judges will be able to recognize conflicts and recuse themselves. This argument has

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92 See Model Rules of Professional Conduct (“MRPC”), Rule 1.1 (Competence).
93 Since no current proposal for expanded TPLF disclosure includes any preservation of privilege, it must be presumed that parties are waiving privilege with regard to the documents disclosed. By definition, then, a lawyer will have to provide adequate counsel to secure from her client informed consent for disclosure if it would lead to the waiver of evidentiary privileges or the release of confidential information protected under MRPC 1.6.
94 MRPC Rule 3.3: Candor Toward The Tribunal
   (a) A lawyer shall not knowingly:
      (1) make a false statement of fact or law to a tribunal or fail to correct a false statement of material fact or law previously made to the tribunal by the lawyer;
96 See Standing Committee Report at 249.
found some traction in parallel debates that have occurred in international arbitration. The parallel with international arbitration is not very useful, however, since international arbitration employs neutral decision-makers who are often drawn from practice, and who may have direct professional relations with TPLF firms. Judges in the United States, on the other hand, while sometimes connected to practice through previous employment, more often face recusal based on financial interests such as ownership of shares in a corporation whose interests will be affected by the outcome of a case before the judge. Given the very small size of the TPLF market, and the even smaller number of publicly traded TPLF firms, the risk of financial interest through shareholding or other forms of investment among judges seems extremely low, and as yet, no one has produced any data to suggest that it is a problem of such scale that special amendments to existing law are required to address it.

A second benefit that has been cited is the specific role that disclosure of TPLF may play in insuring that a court may evaluate a lead counsel with complete information about its financial resources. This argument was the reason that the Northern District of California changed it local rules in connection with class action. It is hard to know whether class members will truly benefit from the new rule. Obviously, it is in no one’s interest for a class to have inadequately capitalized counsel appointed, and to the extent that the rule causes a court to appoint a different lead counsel who would secure a better result for the class, the benefit, even if marginal, may exist. To the extent that the rule is used tactically by defendants to defeat the appointment of class counsel where none takes its place, it is not clear that the rule does work to the advantage of potential class members.

The remaining benefits seem to be directed towards using disclosure as a vehicle for the deterrence of conduct which is prohibited already under existing law. The argument that TPLF disclosure will expose violations of the prohibition of champerty in those states in which it is prohibited does not rely on the claim that disclosure will help improve the integrity of proceeding in which the disclosure occurs, but that it will help prevent wrongdoing that should never have been connected with the proceeding anyway. The same point can be made about the putative benefit of disclosure with regard to violations of the rules of professional responsibility by lawyers who allow third parties to interfere with their independent professional judgment in violation of MRPC 5.4(c).

TPLF can be provided without a lawyer violating her obligation of independent

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97 See Maria Choi, Third-Party Funders in International Arbitration: A Case for Protecting Communication Made in Order to Finance Arbitration, 29 GEO. J. LEGAL ETHICS 883, 889 (2016) (“In response to the rising concerns about conflicts of interest, the IBA Guidelines on Conflicts of Interest were revised in October 2014 to include reference to third-party funders.”).


99 MRCP Rule 5.4: Professional Independence Of A Lawyer

(c) A lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services.
professional judgment to her client, and it is not clear why the exiting law – including the existing mechanisms for the discipline of lawyers who violate their obligations to the bar – are not sufficient to address violations of Rule 5.4(c), to the extent that they arise in the context of TPLF. 100

IV. Conclusion and Recommendations

Argument for most disclosure rules in TPLF face two challenges. First, the problems the proposed rules aim to solve are not ones that seem important or pressing. For example, the risk that judicial conflict of interest due to stock ownership by judges in TPLF companies seems, at this point, mostly in the imagination of the proponents of the disclosure rules. Second, the costs of compliance with the disclosure rules may be large depending on how the rules are framed and interpreted. As a result, the best course of action is caution; both in supporting disclosure and in designing disclosure rules. This paper will conclude by making two recommendations.

1. Make Disclosure Work For Consumers

The most serious criticism of consumer TPLF is that consumers are not getting as much from their transactions with TPLF firms as they could. Proposals to set a price for how much a consumer TPLF firm must pay for a contingent portion of a consumer’s litigation outcome are a form of price control, and price controls are often the last resort for those seeking to protect consumers. (Usury law is a form of price control.) There is no reason to believe – at this point – that markets cannot operate to set prices in this part of consumers’ lives as they do in other parts of their lives. However, for markets to work, there must be transparency and information, and the current consumer TPLF sector lacks both.

Most consumer TPLF contracts are not transparent, since they include many contract terms that are difficult for consumers to understand and compare in order to shop around for the best deal for their lawsuit. 101 Simple pricing – without additional terms such as application fees which are paid only if the consumer’s application is accepted by the funder and the lawsuit is eventually successful – would help consumers know how much the transaction will earn them, so that they can, if they wish, comparison shop. While some disclosure reforms supported by the TPLF industry call for disclosure, disclosure rules could go further by prohibiting certain pricing devices that could be replaced by simpler pricing mechanisms.

100 It should be observed that violations of Rule 5.4(c) have been documented in the context of liability insurance contracts. See Douglas R. Richmond, Walking a Tightrope: The Tripartite Relationship Between Insurer, Insured, and Insurance Defense Counsel, 73 Neb. L. Rev. 265, 283 (1994)). Despite the well-documented risk of a lawyer violating her obligation to provide the client with independent professional judgment, Rule 26 was not amended to deal with that issue – just the issue of conflicts of interest and recusal.

101 See Avraham & Sebok, An Empirical Investigation of Third Party Consumer Litigation Funding, supra note 51.
2. Disclosure to the Court Should Be Limited and In Camera

To the extent that disclosure in commercial TPLF and TPLF in class actions and MDLs is valuable, it should be limited to the audience who needs to be informed: the court. None of the arguments presented by advocates for broad disclosure justify disclosure of funding documents to adverse parties. The cost of such disclosure has been reviewed above, and, while that cost can be contained, there seems to be no reason for the typical plaintiff to bear that cost at all. A simpler solution is to allow the court – and only the court – to examine the facts of the funding relevant to the court’s needs and to determine, based on that preliminary inquiry, whether broader disclosure is warranted.

A good example of targeted disclosure is the order issued on May 7, 2018 in \textit{In Re: National Prescription Opiate Litigation}. Judge Dan Aaron Polster ordered any attorney who has obtained litigation financing to submit, ex parte and in camera, the identity of the financer and to affirm that the financing does not create any conflict of interests, undermine counsel’s obligation of vigorous advocacy, affect counsel’s independent judgment, give the lender any control over litigation strategy or settlement decisions and affect party control of any settlement. The order left open the possibility that discovery by adverse parties into TPLF agreements could occur under “extraordinary circumstances”. Judge Polster’s order is a good model for future legislation, but it also lares bare the weakness of the argument for law reform addressing disclosure of TPLF. At the most, legislation implementing Judge Polster’s order would provide judges with another tool to monitor conflicts of interest. The meaning of “extraordinary circumstances” in Judge Polster’s order is not clear, and although future opinions may illuminate it, it is unlikely that the Judge intended this caveat to take up much of the court’s time or produce significant benefits for the parties. In other words, Judge Polster’s additional disclosure requirements are modest in both ambition and significance. They deserve support, but they are not intended to achieve more than a marginal increase in protection for the integrity of the judicial process. This is not a criticism of Judge Polster’s order, but a recognition that an objective study of the issues raised by TPLF in MDLs entails the conclusion that there is little need for more than minor reform with regard to disclosure of TPLF.

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102 MDL Docket No. 2804, No. 17-md-2804 (N.D. Ohio, Eastern Div.).

103 \textit{Ibid.} The order also held that the work product doctrine could preserve privilege over certain communications between the plaintiffs and third party funders. \textit{Ibid at 2, citing Lambeth Magnetic Structures, LLC v. Seagate Tech. (US) Holdings, Inc.}

104 \textit{Id.}