

## **Ethical Issues in Third Party Litigation Finance**

**Type of Event: CLE (Symposium)**

**Title: Third Party Litigation Finance in the United States**

**Date: February 19, 2011**

**Location: Northern Kentucky University, Chase College of Law**

*For a presentation of the Symposium see [http://chaselaw.nku.edu/spring\\_symposium.php](http://chaselaw.nku.edu/spring_symposium.php)  
(last visited March 18, 2011)*

Main points of Prof Crystal's speech:

- **Will third party litigation finance increase the litigation?** Unlike some economists (e.g. Prof. Paul H. Rubin), I do not think that third party litigation finance will have the effect to increase litigation. In fact, third party litigation finance might lead to more lawsuits (because people or companies that could not afford to file a lawsuit, might be able to because they obtain a financing) but this possibility will be more than outweighed by the faster and fairer settlements of claims. Both sides will know that the each side will have the financial resources to try the case if necessary. As the Supreme Court put it “[W]e cannot endorse the proposition that a lawsuit, as such, is an evil.” *Zauderer v. Office of Disciplinary Counsel*, 471 U.S. 626, 643 (1985).
- **Is third party litigation finance similar to defendant's insurance?** Litigation finance levels the playingfield with defendant. Defendants have insurance that may fully protect them against liabilities and cover the cost of litigation, at least in substantial part. Plaintiffs do not have the possibility of a full insurance coverage. Plaintiffs only have the contingent fee system, which reduces the amount of their recovery instead of reducing their cost of litigation.
- **Should the third party litigation finance be prohibited because of the champerty doctrine?** Champerty is an outmoded doctrine that should be abolished and has in fact been abolished by a number of courts, including the South Carolina Supreme Court. If there are evils associated with litigation finance (for example arguably a third party financier's control of the litigation), they should be dealt directly and not by using the doctrine of champerty.
- **What conflict rules apply?** The rules of the jurisdictions in which the case is pending controls, according to the ABA Model Rule 8.5(b)(1).
- **Is there an ethical issue of fee division in connection with litigation finance?** It depends on the structure of the transaction. The most common ways in which the

financing occurs are: (i) sale of claim, (ii) loan to a party; (iii) loan to a law firm. While no. (i) and no. (ii) do not involve any issue of fee splitting, no. (iii) might, depending on the terms of the loan. For example ordinary loan transaction to a law firm do not involve fee splitting. No (iii), however, might involve a problem of champerty (where not abolished).

- **What is the impact of third party litigation finance on confidentiality, attorney-client privilege and work product doctrine?** Litigation finance does not raise a problem of breach of confidentiality. In fact the client gives informed consent to the disclosure. Litigation finance, however, can raise issues of waiver of attorney-client privilege and work product doctrine. A Florida court (only case that I am aware of) held that the disclosure of information to a third party financier amounts to a waiver. I disagree with this decision. As for the attorney-client privilege there is no waiver because of the common interest exception. As for the work product doctrine, there is no waiver because when a party discloses information under circumstances under which it is unlikely that the adversary will have access to the information it does not amount to a waiver of the work product.
- **Should it be permissible to transfer the right to settle?** While it would be impermissible for a third party financier to interfere with the relationship between a client and his counsel, I question whether it is improper for a client to contract away the right to settle (i.e. to agree that the right to settle the claim pertains to the third party financier). By way of analogy, think that insurance companies typically control the right to settle non-professional liability insurance claims. Besides, if a client could transfer the right to settle by transferring the entire claim, why should not the client have the right to transfer the right to settle when the client has sold a portion of the claim?
- **Is there any issue of interference with professional judgment?** The problem of control might be an issue both in case of a financing through a loan to a party and through loan to a law firm. While the control through the financing leverage is admissible (for example it is obvious that a financier can choose to stop financing if financier does not think that going on with a lawsuit is advisable) the general view is that professional judgment issues should stay with the lawyer and his client. However, I raise issues that sophisticated parties might not contract otherwise.
- **Is there any issue in the financing of class actions?** I do not think that there is problem in the financing of a class action. In the case of a class action the concern of third party financier's overreaching is even diminished because of the court's control on the class action.
- **Should a regulation be passed on third party litigation finance to protect the financed party from overreaching?** I do not think that a regulation should be passed to

protect sophisticated parties. The principle is here freedom of contracts. I would not disagree on a regulation of some sort in case of consumers. I wonder whether a simple disclosure obligation might be effective, however.

- **Should finance agreements be disclosed in court?** It has been suggested that finance agreements should be compulsory disclosed in court. I do not disagree on this kind of suggestion as an analogy with the insurance situation. I also think that the disclosure of the finance agreement might be an incentive to settlements because each party would know that the other party has the resources to proceed with the case.

For more information, you are welcome to write to [info@nathancrystal.com](mailto:info@nathancrystal.com).