Traditionally, the costs of a lawsuit, including legal fees and "case costs," have been funded either by the client, the lawyer, or some combination of these two. The exact method of funding depended on the agreement of the parties. For example, in the traditional personal injury contingent fee case, when the lawyer advances expenses repayment of which are contingent on recovery (ethically proper under SCRPC 1.8(e)), the lawyer bears almost all of the economic risk of the case. However, depending on the relative willingness/ability to pay of the client and the lawyer, risks can be allocated in a different way. For example, in a commercial case the engagement of plaintiff's counsel might provide for a combination of a reduced hourly rate and a reduced contingency fee coupled with the client paying all of the expenses in the case.

In the last 10 years methods of financing litigation and of allocation of risk have grown dramatically with the development of third party litigation finance. See Sara Randazzo, Litigation Financing Attracts New Set of Investors, Wall St. J. (May 15, 2016). For a "cut" of the action, litigation funders can provide financing to lawyers or their clients, thus reducing both the cost and risk of litigation to lawyers and clients. The American Bar Association's 20/20 Commission signaled the importance of this development when it issued a white paper on the topic of "alternative litigation finance." The Commission did not recommend any rule changes or new rules to deal with this development, but it warned lawyers that they must comply with traditional principles of professional conduct when representing clients in connection with transactions involving alternative litigation finance. With the growth of this field, it is incumbent on lawyers to have familiarity with the structure of litigation funding and the risks and benefits of such transactions both to clients but also to lawyers themselves.

**Structure of Litigation Finance Transactions.** Broadly speaking litigation finance falls into two categories: consumer and commercial. In the typical consumer litigation finance transaction, the funder makes a loan or purchases the claim of a plaintiff with repayment to the lender coming from any recovery in the case. Since the funder is bearing all or almost all of the risk, the "cost" of the loan or the discount on the sales price can be substantial. The recent case of Maslowski v. Prospect Funding Partners, LLC, 890 N.W.2d 756 (Minn. Ct. App. 2017), is illustrative. Masklowski, who was injured in an automobile
accident, needed living expenses after she filed suit. She entered into an agreement with Prospect under which Prospect paid Maslowski $6000 in exchange for her agreement to repay Prospect out of any recovery she might obtain the $6000, plus 60% interest and a processing fee of $1425. It is interesting to note that ethics rules foster third party consumer litigation finance because the rules only allow lawyers to make loans to clients for litigation expenses, thus prohibiting lawyers from lending living expenses to their clients. See ABA Model Rule 1.8(e). Without this rule some lawyers would advance living expenses to needy clients; indeed, it is likely that such loans would be on more favorable terms than the 60% interest payment that Maslowski agreed to make. In fact, in some jurisdictions, lawyers are allowed to make loans to clients for living expenses. See DC Rule of Prof. Cond. 1.8(d)(2). In consumer litigation finance, plaintiffs' lawyers play a somewhat passive role; the agreement is between lender and client. Lawyers may provide information to the lender with client consent (but note the impact on the attorney-client privilege discussed below) and may counsel clients about the advantages and disadvantages of such arrangements. See SCRPC 2.1.

In commercial litigation finance, on the other hand, lawyers are intimately involved. Commercial litigation finance may involve a single case or a portfolio of similar cases held by a law firm. For example, financing of a single case might be structured as follows: the lender pays 50% of the law firm's legal fees in exchange for 20% of the recovery in the case; the law firm agrees to receive 50% of its fees as billed and 20% of the recovery in the case; the client pays out-of-pocket expenses, retaining 60% of the recovery. Thus, the law firm, the financier, and the client all have a financial stake in the case. Variations are possible to enable the law firm to be paid a higher portion of its fees or to reduce or perhaps eliminate the client's payment of expenses. See 33 ABA Law. Man. Prof. Cond. 154. In portfolio financing the lender provides capital to the law firm, which is repaid from the proceeds of any cases in the firm's portfolio of cases that are subject to the financing agreement.

Litigation financing presents a number of ethical issues for lawyers.

Champery. The first issue that must be considered regardless of the form of transaction is whether the transaction amounts to "champery." The common-law doctrine of champery provides that a contract to finance or carry the expense of litigation in exchange for an interest in the suit is invalid. In Osprey, Inc. v. Cabana Ltd. Partnership, 340 S.C. 367, 532 S.E.2d 269 (2000), the SC Supreme Court abolished champery as a defense to a contract to finance a lawsuit. The Court reasoned that the historical basis for the doctrine no longer exists and the evils of financing litigation for improper purposes can be controlled in other ways. Osprey does not deal with the related offense of barratry (incitement of litigation), which South Carolina prohibits by statute. S.C. Code Ann. § 16-17-10 et seq. Litigation finance rarely involves barratry because the client almost always has a dispute before the financier becomes involved.

Other states may continue to recognize champery or may have enacted legislation otherwise prohibiting or limiting litigation finance. For example, Minnesota follows the common law rule prohibiting champery. See Johnson v. Wright, 682 N.W.2d 671, 677-78 (Minn. Ct. App. 2004), appeal dismissed (Jan. 10, 2005). Ohio has enacted statutory protection of consumers entering into litigation finance agreements. See Ohio Rev. Code Ann. § 1349.55 (non-recourse civil litigation advance contracts).

Last year the New York Court of Appeals held that a purchase by an off-shore shell company of notes that were in default when the payment of the purchase price was contingent on recovery by the shell company violated the New York champery statute, N.Y. Jud. L. 489, which prohibits the acquisition of notes, securities, and other choses in action "with the intent and for the purpose of bringing an action or
proceeding thereon." See Justinian Capital SPC v. WestLB AG, 65 N.E.3d 1253 (N.Y. 2016). While the case at first blush seems to be adverse to litigation funding, the opposite is actually the case. First, in enacting section 489 the New York legislature intended to abolish the common law doctrine of champertory. Id. at 1259 (Stein, J. dissenting). Thus, litigation finance transactions that do not involve the purchase or assignment of choses in action are not champertous under New York law. Second, even under the statute a purchase or assignment is only champertous if the primary purpose of the transaction was to enable the assignee to bring suit. For example, if the assignment or purchase was in connection with a bona fide business purpose, such as acquisition of a business, the transaction is not champertous. See Fairchild Hiller Corp. v. McDonnell Douglas Corp., 270 N.E.2d 691 (N.Y. 1971). Financing of litigation is a legitimate business purpose, and any litigation to enforce collateral given in connection with the [*14] financing agreement would not be champertous. Finally, the New York statute exempts transactions in which the purchase price is greater than $500,000. In Justinian Capital the court found that the exception did not apply because Justinian Capital did not make an actual payment, and any payment by it was contingent on recovery in the underlying litigation. In litigation finance transactions the lender is always making a payment, so in any commercial litigation finance transaction in which the amount financed is greater than $500,000 the exception should apply.

Since the enforceability of a litigation finance agreement may depend on which state's law is applicable, a well-drafted litigation finance agreement should include choice of law and choice of forum provisions. However, the enforceability of such provisions may be questionable. In Maslowski v. Prospect Funding Partners, LLC, supra, the litigation finance agreement had both a New York choice of law and a New York forum selection clause. Maslowski brought suit in Minnesota claiming that the agreement was void; as noted above Minnesota still recognizes champertory as a defense to an agreement. She sought an injunction to prevent Prospect Funding from enforcing the agreement in New York. The Minnesota court of appeals affirmed the trial court's decision to grant the injunction on the ground that the choice of law/forum clauses were invalid in that they violated a strong Minnesota public policy.

**Attorney-client privilege.** Lawyers have an ethical duty to protect the confidentiality of client information and to only reveal such information with the informed consent of their clients. SCRPC 1.6(a). Clients or lawyers seeking to obtain litigation finance must consider the impact of providing information to the lender on the attorney-client evidentiary privilege. If the client, or the lawyer with the client's consent, provides specific information about the client's case to a litigation financer, the attorney-client privilege is probably lost. The privilege requires that information be conveyed in confidence between lawyer and client or their agents for the purpose of obtaining legal advice. Restatement (Third) of the Law Governing Lawyers § 68. The presence of a third party who is not the agent of either the lawyer or the client jeopardizes the privilege because the communication is no longer in confidence. (It would be difficult to claim that the financer is an "agent" of the client since the financer makes independent financing decisions.) Moreover, lenders are not providing legal advice to the clients. However, if the litigation finance transaction is structured as portfolio financing, it may be possible to maintain the privilege if the lender only receives aggregate information about the portfolio of cases. Even if the attorney-client privilege does not apply, information provided by the client or lawyer to the litigation financer may be protected from disclosure by other doctrines, as will be discussed in Part II of this column.