LAKE WHILLANS

Litigation Finance Ethics Primer

Raising the Prospect of Litigation Finance with Clients

In general, a lawyer can (but it is not obligated to) raise the prospect of litigation funding to a client who may lack funds or wants to hedge litigation risk (the two most off-cited reasons to seek litigation finance per our survey). As the American Bar Association's Commission on Ethics 20/20 put it in its informational report on litigation finance, "if it is legal for a client to enter into the transaction, there would appear to be no reason to prohibit lawyers from informing clients of" the existence of litigation finance companies or referring clients to particular litigation funders. The lawyer should disclose the potential conflict between her interest in having her fees paid and the client's choice to use litigation funding, disclose any relationship with a funder, and obtain informed consent as necessary.

But What About Champerty?

The prohibition on champerty–which has been defined by the U.S. Supreme Court as "[helping another prosecute a suit] in return for a financial interest in the outcome"– is fading in the United States where it ever existed at all. Federal law never adopted the prohibition; neither did states such as California and Texas. Other states, such as Massachusetts, adopted the prohibition on champerty but have since abolished the concept entirely. Others, like New York and Illinois, now construe the prohibition on champerty so narrowly that it would not normally apply to commercial litigation funding arrangements. As one of the last major legal centers to provide clarity on the issue, a Delaware court ruled last year that its champerty doctrine did not apply to a commercial funding arrangement. However, there exists a minority of states where the prohibition may still exist and questions remain as to whether it would apply to commercial financing arrangements; you should expect that any funder will examine the legal landscape in a particular jurisdiction before funding.

Attorney Client Privilege and Work Product Protection

Communications with a funder are not per se protected by the attorney-client privilege, since the financier, while often comprised of trained attorneys, is not acting as the client's legal counsel. There is an unsettled question as to whether the common interest exception would nonetheless apply; courts that have considered it have split on this issue. Thus, at Lake Whillans, we request that communications that are only protected by the attorney client privilege not be shared with us.

However, most communications with a litigation funder or attorney analysis that would be pertinent to the funder's analysis are protected from disclosure by the work product doctrine. Courts have repeatedly held this protection applies to communications with funders, particularly where there is an agreement in place to maintain confidentiality (since work product protection is negated for those communications that could foreseeably be shared with one's adversary).

The Delaware Court of Chancery examined this issue in depth in 2015 and held in Carlyle Investment Management LLC v. Moonmouth Company SA that the work product doctrine protected the disclosure of communications regarding a litigation finance arrangement, reasoning that to convince a funder to provide financing, the claim holder would need to convince her of the merits of the case, which would necessarily involve sharing the "lawyers' mental impressions, theories and strategies[.]" Similarly, the terms of the final agreement—such as the financing premium or acceptable settlement conditions—could reflect an analysis of the merits of the case. The Court

Chancery, in an apparent endorsement of the equalizing benefit of litigation funding, further observed:

No persuasive reason has been advanced in this case why litigants should lose work product protection simply because they lack the financial means to press their claims on their own dime. Allowing work product protection for documents and communications relating to third-party funding places those parties that require outside funding on the same footing as those who do not and maintains a level playing field among adversaries in litigation.

Control of Litigation

Lawyers sometimes worry over the degree of control the funder will exercise over the strategy of the case and whether that raises ethical issues. (We at Lake Whillans generally do not contract for the right to control strategy or settlement). The guiding principle here is that the lawyer should exercise independent professional judgement and render candid advice regardless of the involvement of a funder. The Model Rules anticipate that a third party may pay the fees of another (think insurers for example) and instruct that a lawyer shall not permit a person who pays a lawyer for legal services on behalf of another to "regulate the lawyer's professional judgment." Model Rule 4.5(c)

Conclusion

In many ways, the ethical issues raised by litigation finance are not new and lawyers, already well-equipped to navigate them, should not be dissuaded from exploring litigation funding by ethical reservations. We hope next year's survey shows a rise in firsthand users of litigation funding and a decrease in those reluctant to do so. To learn more about these issues, please feel free reach out to us at drucker@lakewhillans.com. We regularly give in-house seminars on the ethics of litigation funding and would be happy to present at your place of business.