

# Access to Cash, Access to Court: Unlocking the Courtroom Doors with Third-Party Litigation Finance

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| Introduction .....   | 198 |
| I. Initiating Litigation.....                              | 202 |
| II. Getting Third Parties to Pay for Litigation .....      | 208 |
| A. The Cause Model.....                                    | 208 |
| 1. Civil Legal Aid Societies.....                          | 209 |
| 2. Law School Clinics .....                                | 211 |
| 3. Law Firm Pro Bono Programs.....                         | 212 |
| 4. Private Public Interest Law Firms .....                 | 214 |
| B. The Profit Model.....                                   | 216 |
| III. Getting More Third Parties to Pay for Court.....      | 218 |
| A. Existing Modes of Finance .....                         | 219 |
| B. New Models of Finance .....                             | 219 |
| 1. Law Firms As Beneficiaries .....                        | 221 |
| 2. Businesses As Beneficiaries .....                       | 222 |
| 3. Contingency Fee Attorneys As Future Beneficiaries ..... | 222 |
| 4. Increased Access to Justice.....                        | 225 |
| IV. Allowing More Third Parties to Pay for Court .....     | 226 |
| A. Champerty and Maintenance.....                          | 226 |
| B. Concerns over Increased Litigation .....                | 228 |
| C. Concerns over Duty of Loyalty and Fiduciary Duty.....   | 229 |
| D. Protecting Confidentiality.....                         | 234 |
| Conclusion.....  | 236 |

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## INTRODUCTION

Litigating a claim in the United States is an expensive affair.<sup>1</sup> Potential plaintiffs must be prepared to pay a host of fees, including court fees, lawyers' fees, bond requirements, and expert witness fees. The accumulation of these fees has created what Judge Richard Posner termed a "liquidity problem" in civil litigation, as potential plaintiffs lack the capital necessary to pursue a claim.<sup>2</sup> This liquidity problem has, in turn, caused an access to justice problem—people with potentially meritorious claims lack the "key to the courthouse door."<sup>3</sup>

Fortunately for potential plaintiffs, several alternative financing schemes exist in the United States whereby someone else pays to litigate a plaintiff's claim, an arrangement that is broadly known as third-party litigation finance (TPLF). Among the several available forms of TPLF,<sup>4</sup> the American form is unique in that plaintiffs can pay for representation through a contingency fee contract, in which the lawyer shoulders the costs of litigation in exchange for a percentage of the settlement.<sup>5</sup> In this system, plaintiffs' attorneys are freely able to pursue as many claims as are presented to them. Nevertheless, they are constrained in the number of cases they pursue by how much capital they have to finance those cases.<sup>6</sup>

Recently, however, the rules of the game have changed, possibly making it harder for plaintiffs' attorneys to litigate claims. For several decades, since the Supreme Court's ruling in *Conley v. Gibson*,<sup>7</sup> a plaintiff could often have her case heard by pleading the most basic elements of her claim—the basic facts of the situation giving rise to the claim (e.g., the plaintiffs name and the date) and the cause of action.<sup>8</sup> The Supreme Court in *Bell Atlantic v. Twombly*<sup>9</sup> and *Ashcroft v. Iqbal*<sup>10</sup> instituted a heightened pleading standard which now requires a more fact-

1. See Elizabeth J. Cabraser, *Apportioning Due Process: Preserving the Right to Affordable Justice*, 87 DENV. U. L. REV. 437, 440 (2010); Brooke D. Coleman, *The Vanishing Plaintiff*, 42 SETON HALL L. REV. 501, 516–19 (2012); Marc Galanter, *The Day After the Litigation Explosion*, 46 MD. L. REV. 3, 9 (1986); Emery G. Lee III & Thomas E. Willging, *Defining the Problem of Cost in Federal Civil Litigation*, 60 DUKE L.J. 765, 769–71 (2010).

2. RICHARD A. POSNER, *ECONOMIC ANALYSIS OF LAW* 783 (8th ed. 2011) ("The solution to this liquidity problem is the contingent fee contract.")

3. Philip H. Corboy, *Contingency Fees: The Individual's Key to the Courthouse Door*, LITIG., Summer 1976, at 27, 27; see *infra* Part II.A, for a discussion on access to justice.

4. See *infra* Part II.

5. ALEXANDER TABARROK & ERIC HELLAND, *TWO CHEERS FOR CONTINGENT FEES* 6–7 (2005); Christopher R. Drahozal, *Arbitration Costs and Contingent Fee Contracts*, 59 VAND. L. REV. 727, 767–68 (2006); Herbert M. Kritzer, *The Wages of Risk: The Returns of Contingency Fee Legal Practice*, 47 DEPAUL L. REV. 267, 270–71 (1998); Ted Schneyer, *Legal-Process Constraints on the Regulation of Lawyers' Contingent Fee Contracts*, 47 DEPAUL L. REV. 371, 376–77 (1998).

6. HERBERT M. KRITZER, *RISKS, REPUTATIONS, AND REWARDS: CONTINGENCY FEE LEGAL PRACTICE IN THE UNITED STATES* 10–14 (2004).

7. See *Conley v. Gibson*, 355 U.S. 41 (1957).

8. See *infra* Part I.

9. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544 (2007).

10. *Ashcroft v. Iqbal*, 556 U.S. 662 (2009).

based claim, imposing on the plaintiff and her attorney the need to engage in costly prefiling investigations to uncover such facts.<sup>11</sup> This requirement might have hampered the ability of plaintiffs' lawyers to deliver access to justice. Academics and practitioners have debated the effect that the heightened pleading standard has had on plaintiffs and potential plaintiffs.<sup>12</sup> An emerging consensus suggests that the new standard has resulted in fewer claims being heard by judges, either because of higher grant rates of Rule 12(b)(6) motions to dismiss for failure to state a claim or because fewer suits are filed.<sup>13</sup> Similar studies suggest that the decrease in litigation has been partially caused by the inability of plaintiffs or plaintiffs' lawyers to afford expensive prefiling investigations to meet the heightened pleading standard.<sup>14</sup> The new pleading standard, it seems, has created a liquidity problem for some plaintiffs' attorneys, making it more expensive and less likely that a plaintiff's attorney will file a case.

This Note suggests that, in light of heightened pleading standards, decreased access to justice, and capital constraints, plaintiffs' lawyers and potential litigants need to search for new ways to finance litigation. Such a fix may already be at hand. Over the last several years, a controversial new model of TPLF has developed that could potentially alleviate the burden imposed by *Twombly* and *Iqbal*.<sup>15</sup> In exchange for a portion of any settlement, financial groups have offered plaintiffs' attorneys cash to fund litigation efforts.<sup>16</sup> Although the practice is regulated and pervasive in Australia,<sup>17</sup> it is largely unregulated and rare in the

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11. See *infra* Part I.

12. JOSHUA CIVIN & DEBO P. ADEGBILE, RESTORING ACCESS TO JUSTICE: THE IMPACT OF IQBAL AND TWOMBLY ON FEDERAL CIVIL RIGHTS LITIGATION (2010), available at [http://www.acslaw.org/sites/default/files/Civin\\_Adegbile\\_Iqbal\\_Twombly.pdf](http://www.acslaw.org/sites/default/files/Civin_Adegbile_Iqbal_Twombly.pdf); see also JOE S. CECIL ET AL., FED. JUDICIAL CTR., MOTIONS TO DISMISS FOR FAILURE TO STATE A CLAIM AFTER IQBAL, at vii (2011) [hereinafter CECIL ET AL., MOTIONS TO DISMISS AFTER IQBAL], available at <http://www.uscourts.gov/uscourts/RulesAndPolicies/rules/Publications/motioniqbal.pdf>; JOE S. CECIL ET AL., FED. JUDICIAL CTR., UPDATE ON RESOLUTION OF RULE 12(b)(6) MOTIONS GRANTED WITH LEAVE TO AMEND 1–2 (2011) [hereinafter CECIL ET AL., UPDATE ON RESOLUTION OF 12(b)(6) MOTIONS], available at [http://www.fjc.gov/public/pdf.nsf/lookup/motioniqbal2.pdf/\\$file/motioniqbal2.pdf](http://www.fjc.gov/public/pdf.nsf/lookup/motioniqbal2.pdf/$file/motioniqbal2.pdf).

13. See Jonah B. Gelbach, *Locking the Doors to Discovery? Assessing the Effects of Twombly and Iqbal on Access to Discovery*, 121 YALE L.J. 2270, 2332 (2012).

14. *Whether the Supreme Court Has Limited Americans' Access to Court: Hearing Before the S. Comm. on the Judiciary*, 111th Cong. 16 (2009) [hereinafter *Americans' Access to Court*] (statement of Stephen B. Burbank, David Berger Professor for the Administration of Justice, University of Pennsylvania), available at <http://www.judiciary.senate.gov/imo/media/doc/12-02-09%20Burbank%20Testimony.pdf>; Scott Dodson, *New Pleading, New Discovery*, 109 MICH. L. REV. 53, 67 (2010).

15. JONATHAN T. MOLOT, THEORY AND PRACTICE IN LITIGATION RISK 6–9 (2012), available at [http://www.burfordcapital.com/wp-content/uploads/2012/11/Burford\\_Whitepaper11.pdf](http://www.burfordcapital.com/wp-content/uploads/2012/11/Burford_Whitepaper11.pdf).

16. STEVEN GARBER, ALTERNATIVE LITIGATION FINANCING IN THE UNITED STATES: ISSUES, KNOWN, AND UNKNOWN 13 (2010), available at [http://www.rand.org/pubs/occasional\\_papers/OP306.html](http://www.rand.org/pubs/occasional_papers/OP306.html); William Alden, *Looking to Make a Profit on Lawsuits, Firms Invest in Them*, N.Y. TIMES, May 1, 2012, at B3; Dan McDonald, *Third-Party Litigation Financing: Is It Really Taking Off?*, R.I. LAW. WKLY. (Feb. 2, 2012), <http://rilawyersweekly.com/blog/2012/02/02/third-party-litigation-financing>.

17. David S. Abrams & Daniel L. Chen, *A Market For Justice: A First Empirical Look at Third*

United States, except for a few notable cases.<sup>18</sup> Perhaps most famously, the plaintiffs' attorney who represented a group of Ecuadorians suing Chevron for environmental claims received over \$4 million in litigation finance from Burford Capital.<sup>19</sup>

Because of the newness and novelty of this practice, attorneys, financiers, and regulators are still exploring and attempting to understand its implications. To date, much of the discussion surrounding the new form of TPLF has focused on either its impact on the attorney-client relationship or on the supply-side dynamics of how investing should be regulated.<sup>20</sup> Little is known, however, about who might benefit from the further expansion of this form of TPLF and how that expansion might occur.<sup>21</sup>

This Note will argue that this new form of TPLF could be expanded to help plaintiffs' attorneys surmount the new pleading standard, thereby increasing access to justice. By providing plaintiffs' attorneys with capital, TPLF might enable them to afford the pre-filing investigations required to survive a motion to dismiss, in the process reopening the courtroom door. But expanding TPLF is not without risks, including the possibility of increased filings of frivolous claims, fraud, and the erosion of the attorney-client relationship. Because of these risks, this Note will further propose a new regulatory regime that should be adopted to ensure that this new form of TPLF can benefit all classes of plaintiffs.

Part I of this Note argues that access to justice is limited by at least two factors: the costs of litigation and a heightened pleading standard. The heightened pleading standard has shifted some costs onto the plaintiff that used to be

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*Party Litigation Funding*, 15 U. PA. J. BUS. L. 1075, 1084 (2013); Nicholas Dietsch, *Litigation Financing in the U.S., the U.K., and Australia: How the Industry Has Evolved in Three Countries*, 38 N. KY. L. REV. 687, 702–05 (2011).

18. See Maya Steinitz, *Whose Claim Is This Anyway? Third-Party Litigation Funding*, 95 MINN. L. REV. 1268, 1289–92 (2011).

19. Patrick Radden Keefe, *Reversal of Fortune*, NEW YORKER, Jan. 9, 2012, at 38.

20. See Courtney R. Barksdale, *All That Glitters Isn't Gold: Analyzing the Costs and Benefits of Litigation Finance*, 26 REV. LITIG. 707, 710–16 (2007); Jason Lyon, *Revolution in Progress: Third-Party Funding of American Litigation*, 58 UCLA L. REV. 571, 575–76 (2010); Susan Lorde Martin, *The Litigation Financing Industry: The Wild West of Finance Should Be Tamed Not Outlawed*, 10 FORDHAM J. CORP. & FIN. L. 55, 56–57 (2004); Jonathan T. Molot, *Litigation Finance: A Market Solution to a Procedural Problem*, 99 GEO. L.J. 65, 104–05 (2010); Maya Steinitz, *The Litigation Finance Contract*, 54 WM. & MARY L. REV. 455, 456 (2012); Mariel Rodak, Comment, *It's About Time: A Systems Thinking Analysis of the Litigation Finance Industry and Its Effect on Settlement*, 155 U. PA. L. REV. 503, 503–04 (2006); A.B.A. Comm'n on Ethics 20/20, *White Paper on Alternative Litigation Finance 15–16* (Draft 2011), available at [http://www.americanbar.org/content/dam/aba/administrative/ethics\\_2020/20111019\\_draft\\_alf\\_white\\_paper\\_posting.authcheckdam.pdf](http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111019_draft_alf_white_paper_posting.authcheckdam.pdf).

21. Joanna M. Shepherd, *Ideal Versus Reality in Third-Party Litigation Financing*, 8 J.L. ECON. & POL'Y 593, 608–09 (2012). To date, only a few studies have investigated who might benefit from an expansion of TPLF. See Bruce L. Beron & Jason E. Kinsella, *David vs. Goliath Patent Cases: A Search for the Most Practical Mechanism of Third Party Litigation Financing for Small Plaintiffs*, 38 N. KY. L. REV. 605, 609 (2011).

incurred by the defendant during discovery;<sup>22</sup> now those costs are carried by plaintiffs who choose to engage in prefiling investigations.<sup>23</sup> Unable to bear these costs, fewer plaintiffs and potential plaintiffs see a claim survive a 12(b)(6) motion. Part II of this Note discusses the various forms of TPLF available to plaintiffs and shows that the inability to pay for the costs of litigation has been a theme of the American courtroom experience.<sup>24</sup> The “cause model” of TPLF—where TPLF is supplied by legal aid societies, the pro bono programs of law firms, and private public interest law firms—has helped litigants with civil rights and constitutional claims reach the courtroom.<sup>25</sup> Plaintiffs whose claims fall outside of the cause model may pursue their claim through a “profit model” of TPLF supplied by contingency fee lawyers. This part concludes with an examination of how institutional constraints placed on each third-party financier have created segmented markets in TPLF, where each financier serves a specific type of plaintiff.

Part III of this Note argues that expansion of TPLF could have a profound impact on contingency fee lawyers, with the further benefit of expanding access to justice. Unlike larger law firms that have lines of credit from banks, contingency fee lawyers generally self-finance litigation. This need to self-finance cases imposes serious capital constraints on plaintiffs’ attorneys. Without access to financing, contingency fee lawyers have typically operated under a “portfolio” business model, whereby settlements from a number of low-risk, low-reward claims provide the capital necessary to finance a small number of high-risk, high-reward claims.<sup>26</sup> Making this new form of TPLF available to a contingency fee lawyer would enable the lawyer to pursue claims that she would otherwise have had to decline because of limited capital; access to increased capital could possibly aid the lawyer’s ability to surmount the additional costs imposed by *Twombly* and *Iqbal*.

Part IV explores the concerns with further expanding this form of TPLF and concludes with suggestions for how the practice could be regulated. Current laws in several states against champerty, which proscribes “maintaining a suit in return for a financial interest in the outcome,” and maintenance, which proscribes “helping another prosecute a suit,” prohibit expansions of TPLF.<sup>27</sup> But many states have not enforced the laws for decades, while others have fully abandoned

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22. See, e.g., ROBERT G. BONE, CIVIL PROCEDURE: THE ECONOMICS OF CIVIL PROCEDURE 217 (2003); Frank H. Easterbrook, *Discovery as Abuse*, 69 B.U. L. REV. 635, 636 (1989).

23. Arthur R. Miller, *Are the Federal Courthouse Doors Closing? What’s Happened to the Federal Rules of Civil Procedure?*, 43 TEX. TECH L. REV. 587, 598 (2011).

24. Stephen C. Yeazell, *Re-financing Civil Litigation*, 51 DEPAUL L. REV. 183, 194–95 (2001).

25. Scott L. Cummings & Deborah L. Rhode, *Managing Pro Bono: Doing Well by Doing Better*, 78 FORDHAM L. REV. 2357, 2359 (2010); Rebecca L. Sandefur, *Lawyers’ Pro Bono Service and American-Style Civil Legal Assistance*, 41 LAW & SOC’Y REV. 79, 80–81 (2007).

26. KRITZER, *supra* note 6, at 12–13.

27. *In re Primus*, 436 U.S. 412, 424–25 n.15 (1978); see also Lyon, *supra* note 20, at 579.

the rules.<sup>28</sup> This lack of enforcement means that the new form of TPLF is largely unregulated in many states. While certain groups, such as the United States Chamber of Commerce, advocate for a full prohibition of investing in lawsuits,<sup>29</sup> a more balanced regulatory regime would ensure that TPLF can benefit a diverse class of plaintiffs.

### I. INITIATING LITIGATION

For decades, the Federal Rules of Civil Procedure (FRCP) required that plaintiffs only had to provide the most basic facts in a complaint to have their claim heard by a judge. After the Supreme Court rulings of *Twombly* and *Iqbal*, plaintiffs had a higher bar to clear and are now required to plead more facts. As this Part will discuss, the higher bar plaintiffs have had to clear post-*Twombly* and *Iqbal* has decreased access to justice. Facts that plaintiffs once gained during discovery—after their claim survived a Rule 12(b)(6) motion to dismiss for failure to state a claim—are now required at the pleading stage. As the costs of discovery are often disproportionately paid for by the defendants, plaintiffs must now engage in costly prefilings investigations to increase their chances of surviving a motion to dismiss. This Part will suggest that this increased cost has kept many from having their day in court.

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Promulgated in 1938 by the Supreme Court, the FRCP ensured that a potential plaintiff who had a claim would have her case heard by a judge.<sup>30</sup> Before 1938, a complaint—the form submitted by a plaintiff to a court stating the plaintiff's claim for relief—had to include “[a] statement of the facts constituting the cause of action.”<sup>31</sup> Exactly which facts had to be included in that statement, however, was vague; “ultimate” facts had to be included in the pleading, while “evidentiary” facts and “conclusions of law” were to be left out of pleadings.<sup>32</sup> The rule drafters worried that these requirements screened cases too early in the

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28. See, e.g., *Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217 (Ohio 2003); *Saldini v. Righellis*, 687 N.E.2d 1224, 1224 (Mass. 1997).

29. See JOHN BEISNER ET AL., *SELLING LAWSUITS, BUYING TROUBLE* 1–2 (2009), available at [http://www.instituteforlegalreform.com/images/stories/documents/pdf/research/thirdparty\\_litigationfinancing.pdf](http://www.instituteforlegalreform.com/images/stories/documents/pdf/research/thirdparty_litigationfinancing.pdf) (“The stranger wants to protect its investment, and its interest lies in maximizing its return on that investment, not in vindicating a plaintiff’s rights.”).

30. Christopher M. Fairman, *The Myth of Notice Pleading*, 45 ARIZ. L. REV. 987, 990 (2003) (citing Charles E. Clark, *The Handmaid of Justice*, 23 WASH. U. L.Q. 297, 318–19 (1938)).

31. Scott Dodson, *Comparative Convergences in Pleading Standards*, 158 U. PA. L. REV. 441, 447 (2009) (quoting Act of Apr. 12, 1848, ch. 379 § 120(2), 1848 N.Y. Laws 521).

32. Kevin M. Clermont & Stephen C. Yeazell, *Inventing Tests, Destabilizing Systems*, 95 IOWA L. REV. 821, 824–25 (2010); Dodson, *supra* note 14, at 57; Richard L. Marcus, *The Puzzling Persistence of Pleading Practice*, 76 TEX. L. REV. 1749, 1752–54 (1998); Richard L. Marcus, *The Revival of Fact Pleading Under the Federal Rules of Civil Procedure*, 86 COLUM. L. REV. 433, 433 (1986) [hereinafter Marcus, *The Revival*].

adjudication process. To remedy the nebulous requirements, the rule drafters scrapped the required factual statement from the pleading. Rule 8(a)(2) of the FRCP required only that plaintiffs plead “a short and plain statement of the claim’ that will give the defendant fair notice of what the plaintiff’s claim is and the grounds upon which it rests.”<sup>33</sup> This short and plain statement, dubbed “notice pleading,”<sup>34</sup> served three purposes: it ensured that a plaintiff would have a day in court, it “inform[ed] the opponent of the affair or transaction to be litigated . . . and [told] the court of the broad outlines of the case.”<sup>35</sup> According to one scholar, the effect of “notice pleading” embodied the “liberal ethos” of the rule drafters,<sup>36</sup> a sentiment that “[p]laintiffs . . . should have ‘the opportunity to present their case to [a] Federal judge even when they [do] not yet have [a] full set of facts.’”<sup>37</sup>

In practice, plaintiffs had to divulge the most basic details of their claim to gain access to a judge. But the task was not an onerous one—plaintiffs had to include the name of the parties, the circumstances, and the cause of action.<sup>38</sup> If the pleading lacked such details, or if the pleading was “so vague or ambiguous that the party cannot reasonably prepare a response,” the defendant could utilize Rule 12(e) to motion to dismiss for a more definite statement.<sup>39</sup> Defendants also had the option to file a Rule 12(b)(6) motion to dismiss for failure to state a claim upon which relief can be granted.<sup>40</sup> But the Supreme Court, in *Conley v. Gibson*, declared that such motions should only be granted if “it appears beyond doubt that the plaintiff can prove no set of facts in support of his claim which would entitle him to relief.”<sup>41</sup> In other words, the Court ruled that Rule 12(b)(6) motions should not be granted simply because a plaintiff failed to plead with factual simplicity. Rather, such a motion should only be granted if the facts do not exist anywhere.

By allowing a claim to proceed past the pleading stage with minimal factual detail, the Court shifted some costs from plaintiff to defendant. When a plaintiff initiates filing a claim, the plaintiff herself likely does not possess all of the facts necessary to carry her claim through trial. Depending on the type of claim, many of the facts that she needs might be in the possession of the defendant or other third parties. But if a court requires a fact-based pleading, gathering those details

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33. *Conley v. Gibson*, 355 U.S. 41, 47 (1957) (quoting FED. R. CIV. P. 8(a)(2)).

34. *Id.*

35. Charles E. Clark, *Simplified Pleading*, 2 F.R.D. 456, 460–61 (1943).

36. Marcus, *The Revival*, *supra* note 32, at 439–40.

37. Diarmuid F. O’Scannlain, *Access to Justice Within the Federal Courts—A Ninth Circuit Perspective*, 90 OR. L. REV. 1033, 1037 (2012) (quoting *Access to Justice Denied: Ashcroft v. Iqbal: Hearing Before Subcomm. on the Constitution, Civil Rights, and Civil Liberties of the H. Comm. on Judiciary*, 111th Cong. 4 (2009) (statement of Henry C. Johnson, Jr., Member, H. Comm. on the Judiciary, Subcomm. on the Constitution, Civil Rights, and Civil Liberties)).

38. FED. R. CIV. P. 8.

39. *Id.* at 12(e).

40. *Id.* at 12(b)(6).

41. *Conley v. Gibson*, 355 U.S. 41, 45–46 (1957).

would require plaintiffs to finance and conduct prefiling investigations. *Conley*, however, abrogated the need for most prefiling investigations. Such details that might have been uncovered during a prefiling investigation would likely be revealed when plaintiffs gained access to discovery—the process through which defendants turn over documents to the plaintiffs after the pleading stage. Unlike a prefiling investigation, through discovery, plaintiffs’ lawyers can get access to important documents and facts without paying significant costs; through discovery, the defendants must marshal all of the documents in the defendants’ possession for the plaintiff.<sup>42</sup> By shifting those costs to the defendants, a plaintiff could access a judge with having paid little more than court filing fees and attorney fees.

The impact of the rulings by the Supreme Court in *Twombly* and *Iqbal*, however, may have shifted those costs back to plaintiffs. In *Twombly*, the Court amended the *Conley* “no set of facts” standard slightly by requiring “enough facts to state a claim to relief that is plausible on its face.”<sup>43</sup> What exactly “plausible” means has proved amorphous.<sup>44</sup> The Court suggested that “plausible” is more than “conceivable” but less than “probable.”<sup>45</sup> But while *Twombly* only slightly changed the pleading standard, the Court in *Iqbal* raised the bar higher by ruling that when a court considers a Rule 12(b)(6) motion to dismiss, the court may weed out conclusory statements from the claim and focus solely on the factual allegations.<sup>46</sup> This ruling requires that plaintiffs make “more than an unadorned, the-defendant-unlawfully-harmed-me accusation” and include facts in their pleading that support such a claim.<sup>47</sup> In making these rulings, the Court attempted to reduce the number of frivolous claims filed while also attempting to limit the imposition of excessive discovery costs on defendants.<sup>48</sup> Such a requirement has the possibility to increase costs for a plaintiff substantially. If a plaintiff was not personally in possession of such facts, a prefiling investigation conducted at their own expense would be necessary.

One recent slip-and-fall negligence case demonstrates how a judge dismissed

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42. BONE, *supra* note 22, at 217; Robert G. Bone, *Twombly, Pleading Rules, and the Regulation of Court Access*, 94 IOWA L. REV. 873, 884 n.56, 933–34 (2009); Easterbrook, *supra* note 22, at 636; Charles Silver, *Does Civil Justice Cost Too Much?*, 80 TEX. L. REV. 2073, 2093 (2002); Yeazell, *supra* note 24, at 194–95.

43. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007).

44. Countless articles have attempted to dissect the meaning of the rulings. *See, e.g.*, Benjamin P. Cooper, *Iqbal’s Retro Revolution*, 46 WAKE FOREST L. REV. 937, 938 n.7 (2011).

45. *Twombly*, 550 U.S. at 570; *see also* Clermont & Yeazell, *supra* note 32, at 826.

46. *Ashcroft v. Iqbal*, 556 U.S. 662, 679 (2009).

47. *Id.* at 677. According to one scholar, *Iqbal* completely rejected the *Conley* standard by requiring that “a claim must always be properly supported by factual detail alleged in the complaint. Other facts uncovered in discovery may be used to support the claims, but the complaint itself must be able to stand on its own allegations.” Dodson, *supra* note 14, at 62.

48. Clermont & Yeazell, *supra* note 32, at 850.



a plaintiff's claim through a Rule 12(b)(6) motion due to a lack of facts in the pleading. In June 2007, Holly Branham visited a Dollar General Store in Amherst County Virginia.<sup>49</sup> Branham alleged in her complaint that once in the store, she slipped and fell on liquid pooled on the store's floor, that she suffered injuries—severe and permanent—because of the fall, and that the defendant negligently failed to remove the liquid or to warn her of its presence.<sup>50</sup> Under the old notice pleading regime, this complaint contained all of the components needed to survive a Rule 12(b)(6) motion to dismiss. Indeed, the complaint is nearly identical to the illustrative civil rules forms that accompany the FRCP.<sup>51</sup> Judge Norman Moon, however, granted the defendant's Rule 12(b)(6) motion to dismiss because “the Plaintiff ha[d] failed to allege any facts that show[ed] how the liquid came to be on the floor, whether the Defendant knew or should have known of the presence of the liquid, or how the Plaintiff's accident occurred.”<sup>52</sup> Judge Moon, however, gave Branham fifteen days to amend the complaint<sup>53</sup> and to submit a “well-pleaded factual allegation[.]” as required by *Iqbal*.<sup>54</sup> Branham's amended complaint, which survived all Rule 12 motions, contained greater factual detail uncovered during the prefiling investigation, including the name of the worker at the store, details of the conversation between the plaintiff and defendant's employee, and the conditions within the store at the time of the accident.<sup>55</sup>

The effect of the need for prefiling investigations is only now being understood. Several studies conducted shortly after the *Iqbal* ruling suggest that the heightened pleading standard has had no effect on litigants. One study undertaken by the Federal Judicial Center (FJC) that examined the grant rates of Rule 12(b)(6) motions in the years before and after *Twombly* noted that “[t]here was no increase from 2006 to 2010 in the rate at which a grant of a motion to dismiss terminated the case.”<sup>56</sup> More recent studies, however, have attacked the thinness of the FJC study. One such study found that the heightened pleading standard has resulted in roughly twenty percent fewer plaintiffs surviving Rule

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49. Complaint at 1, *Branham v. Dolgencorp, Inc.*, No. 6:09-CV-00037 (W.D. Va. June 30, 2009).

50. *Id.*

51. See FED. R. CIV. P. FORM 11. While the filer of the complaint must also include statements for diversity jurisdiction, federal question jurisdiction, and admiralty or maritime jurisdiction, the pleading component of the illustrative civil rules form only states “[o]n <Date>, at <Place>, the defendant negligently drove a motor vehicle against the plaintiff. As a result, the plaintiff was physically injured, lost wages or income, suffered physical and mental pain, and incurred medical expenses of \$ <\_\_\_\_>. Therefore, the plaintiff demands judgment against the defendant for \$ <\_\_\_\_>, plus costs.”

52. See *Branham v. Dolgencorp, Inc.*, No. 6:09-CV-00037, 2009 WL 2604447, at \*2 (W.D. Va. Aug. 24, 2009).

53. *Id.*

54. *Ashcroft v. Iqbal*, 556 U.S. 662, 679 (2009).

55. Amended Complaint at 1, *Branham v. Dolgencorp, Inc.*, No. 6:09-CV-00037 (W.D. Va. Aug. 9, 2009).

56. CECIL ET AL., MOTIONS TO DISMISS AFTER IQBAL, *supra* note 12, at vii; see also CECIL ET AL., UPDATE ON RESOLUTION OF 12(b)(6) MOTIONS, *supra* note 12, at 1.

12(b)(6) motions, with an unknown number of plaintiffs simply choosing not to file.<sup>57</sup>

Another recent study found that the heightened standard has had a disparate impact depending on the types of case filed.<sup>58</sup> The study drew on a database that included 500 randomly selected cases submitted in the two years before *Twombly* and 500 cases submitted in the year period after *Iqbal*.<sup>59</sup> Claims based on constitutional civil rights suffered the most under *Iqbal* when compared to their fate under *Conley*; courts after *Iqbal* granted Rule 12(b)(6) motions with and without leave to amend sixty-four percent of the time. Under the *Conley* standard, the similar grant rate was forty-one percent. Other classes of claims suffered similar setbacks: Rule 12(b)(6) motions with and without leave to amend filed against Employee Retirement Income Security Act (ERISA) and Fair Labor Standards Act (FLSA) claims under *Conley* were granted thirty-seven percent of the time and sixty percent of the time under *Iqbal*; for consumer credit claims, the motions were granted thirty-six percent of the time under *Conley* and seventy-two percent of the time under *Iqbal*; and for contract claims, the motions were granted twenty-five percent of the time under *Conley* and thirty-three percent of the time under *Iqbal*.<sup>60</sup>

Exactly why plaintiffs fail to meet the new pleading standard is unclear. While some plaintiffs likely fail to survive a Rule 12(b)(6) motion because the facts they need are held by a party who does not have to turn over requests for information before discovery,<sup>61</sup> other plaintiffs likely fail to survive a Rule 12(b)(6) motion because “they lack the resources to engage in extensive pre-filing investigation[s],”<sup>62</sup> as was perhaps the case for Branham noted above.

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57. Gelbach, *supra* note 13, at 2332; *see also* Dodson, *supra* note 14, at 67; Patricia W. Hatamyar, *The Tao of Pleading: Do Twombly and Iqbal Matter Empirically?*, 59 AM. U. L. REV. 553, 597–602, 614 (2010); Lonny Hoffman, *Twombly and Iqbal’s Measure: An Assessment of the Federal Judicial Center’s Study of Motions to Dismiss*, 6 FED. CTS. L. REV. 1, 32 (2012).

58. Patricia Hatamyar Moore, *An Updated Quantitative Study of Iqbal’s Impact on 12(b)(6) Motions*, 46 U. RICH. L. REV. 603, 609 (2012) (providing difference from *Conley* to *Iqbal* for motions granted in full with and without leave to amend went from forty-six percent to sixty-one percent).

59. Hatamyar, *supra* note 57, at 584–89. The updated database thus includes 1326 cases: 444 decided under *Conley*, 422 decided under *Twombly*, and 460 decided under *Iqbal*.

60. Moore, *supra* note 58, at 626–27. The study included information on others types of claims filed (e.g., tort and intellectual property), but the results were not statistically significant. *Id.* at 618.

61. Damon C. Andrews, *Iqbal-ing Seagate: Plausibility Pleading of Willful Patent Infringement*, 25 BERKELEY TECH. L.J. 1955, 1966–67 (2010); Raymond H. Brescia, *The Iqbal Effect: The Impact of New Pleading Standards in Employment and Housing Discrimination Litigation*, 100 KY. L.J. 235, 254–78 (2012); J. Scott Pritchard, *The Hidden Costs of Pleading Plausibility: Examining the Impact of Twombly and Iqbal on Employment Discrimination Complaints and the EEOC’s Litigation and Mediation Efforts*, 83 TEMP. L. REV. 757, 775–89 (2011); Elizabeth M. Schneider, *The Changing Shape of Federal Civil Pretrial Practice: The Disparate Impact on Civil Rights and Employment Discrimination Cases*, 158 U. PA. L. REV. 517, 524–26 (2010).

62. *Americans’ Access to Court*, *supra* note 14, at 16.

The costs of pre-filing investigations, however, burden the already liquidity-strained litigant. A potential plaintiff must be prepared to pay a host of fees if she chooses to file a claim in the United States. These costs include the court fees to file the case, the hourly fees of a lawyer who will litigate on behalf of the plaintiff, fees to pay expert witnesses if her case calls for it, and other possible fees depending on the type of claim she is filing.<sup>63</sup> The sum of these fees has created what Judge Richard Posner termed “a liquidity problem,”<sup>64</sup> in which plaintiffs with potentially meritorious claims cannot afford to bring those claims to court due to capital constraints. Other scholars have expressed concern over how systemic this liquidity problem has become. Scott Cummings, in a study of how liquidity-strained plaintiffs access the courts, similarly noted that there is a “market inequality” in the availability of legal services.<sup>65</sup> As Cummings wrote, “individuals, despite suffering a legal harm, are blocked from legal redress because they are too poor to pay for a lawyer.”<sup>66</sup>

And as Judge Moon’s opinion above indicates, the new pleading standards set by *Twombly* and *Iqbal* can serve as a barrier to justice for the most basic legal claims. While *Twombly* involved an antitrust claim against telephone companies<sup>67</sup> and *Iqbal* involved a torture claim against the Attorney General of the United States and the director of the Federal Bureau of Investigation,<sup>68</sup> *Branham* was a simple slip-and-fall case.<sup>69</sup> While the heightened pleading standards set by the Supreme Court in *Twombly* and *Iqbal* only apply to actions filed in federal courts,<sup>70</sup> many state courts, where ninety-five percent of claims are filed,<sup>71</sup> have also adopted the standard. To be sure, one study of pleading standards in state courts reveals that the seven states that replicate the FRCP for actions filed in state courts have adopted the *Twombly* and *Iqbal* standard; five other states that do not

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63. Martin Gramatikov, *A Framework for Measuring the Costs of Paths to Justice*, J. JURIS, Feb. 2009, at 111, 116; David M. Trubek et al., *The Costs of Ordinary Litigation*, 31 UCLA L. REV. 72, 92–94 (1983).

64. POSNER, *supra* note 2, at 783.

65. Scott L. Cummings, *The Pursuit of Legal Rights—and Beyond*, 59 UCLA L. REV. 506, 523 (2012).

66. *Id.*

67. *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 550 (2007).

68. *Ashcroft v. Iqbal*, 556 U.S. 662, 666 (2009).

69. *Branham v. Dolgencorp, Inc.*, No. 6:09-CV-00037, 2009 WL 2604447, at \*1 (W.D. Va. Aug. 24, 2009).

70. A. BENJAMIN SPENCER, PLEADING IN STATE COURTS AFTER TWOMBLY AND IQBAL 10 (2010), available at <http://ssrn.com/abstract=2038349> (reporting that all of the federal circuits have “embraced [*Twombly* and *Iqbal*] with zeal”).

71. Compare R. LAFOUNTAIN ET AL., COURT STATISTICS PROJECT, EXAMINING THE WORK OF STATE COURTS: AN ANALYSIS OF 2010 STATE COURT CASELOADS 1 (2012), available at [http://www.courtstatistics.org/~media/Microsites/Files/CSP/DATA%20PDF/CSP\\_DEC.ashx](http://www.courtstatistics.org/~media/Microsites/Files/CSP/DATA%20PDF/CSP_DEC.ashx) (listing total number of filings in state courts in 2010), with U.S. CENSUS BUREAU, STATISTICAL ABSTRACT OF THE UNITED STATES 209 tbl.332 (2012), available at <http://www.census.gov/compendia/statab/2012/tables/12s0332.pdf> (listing the number of filings in federal district courts in 2010).

replicate the Federal Rules of Civil Procedure have also mentioned *Twombly* and *Iqbal* during discussions of fact-based pleading standards.<sup>72</sup>

Although *Twombly* and *Iqbal* are relatively new rules, their combined impact has changed the nature of pleading standards and, in effect, changed who can have their claim heard by a judge. A plaintiff, regardless of the monetary size of her claim, regardless of the complexity of her cause of action, and regardless of whether she files her claim in a federal court or state court, can expect to need to plead more facts than she would have needed to plead ten years ago. This need to plead more facts equates to the need to spend more money at the outset of a case. But how is the cash-strapped plaintiff supposed to find the needed money?

## II. GETTING THIRD PARTIES TO PAY FOR LITIGATION

Depending on the type of claim, a cash-strapped plaintiff in the United States might be able to get her claim paid for by someone else through a TPLF arrangement. TPLF is most broadly defined as an arrangement in which a party not privy to a claim assumes the litigation expenses for a party privy to the claim.<sup>73</sup> These arrangements have developed in the United States “in recognition that the ordinary marketplace for legal services fails to provide such services to significant sectors of the population and to significant interests.”<sup>74</sup>

As this part will examine, the third parties that provide financing fall into two broad groups. The first group finances litigation because it hopes the outcome will further a cause (the “cause model”). The financiers include community civil legal aid societies, private public interest law firms, and the pro bono programs at private law firms. The second group finances litigation to generate a monetary return on its investment (the “profit model”). This group is largely populated by contingency fee lawyers. Of the types of claims financiers in each group pursue, institutional constraints limit their efforts. These constraints, which have evolved over the course of the twentieth century, have created a segmented market in third-party litigation finance, where each type of financier services a particular type of plaintiff. Ultimately, however, the interplay of the various constraints have left a subset of plaintiffs without access to financing and, thus, without easy access to courts. This part will begin to make the claim that, because of an expected monetary return on investment, an expansion of TPLF will most benefit contingency fee lawyers.

### A. *The Cause Model*

Litigation finance provided under the cause model is generally given to

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72. SPENCER, *supra* note 70, at 15–17.

73. Lyon, *supra* note 20, at 577; Steinitz, *supra* note 18, at 1275–76.

74. Scott L. Cummings, *Privatizing Public Interest Law*, 25 GEO. J. LEGAL ETHICS 1, 1 (2012).

benefit a single cause or a low-income individual. To understand how the cause model works today, a grasp of how the model developed is necessary.

### 1. *Civil Legal Aid Societies*

The movement toward providing legal services to the poorer sectors of the community began in the late nineteenth century; lawyers donated their services directly to community members who could not otherwise afford to hire a lawyer to settle simple, civil disputes.<sup>75</sup> By the early twentieth century, local community civil legal aid societies, formed through charitable organizations, paid for attorneys to represent indigent clients.<sup>76</sup> The attorneys who participated in the programs often provided their services for a reduced fee or for no fee at all, as a “professional charity.”<sup>77</sup> Through these societies, attorneys “operated as neutral partisans for the poor, advocating for client goals.”<sup>78</sup> By the second decade of the twentieth century, state bars helped expand the programs.<sup>79</sup> While only 40 legal aid societies existed in 1919 in the largest cities, 92 cities had legal aid societies by 1950, and 209 cities by 1960.<sup>80</sup> Then, in 1965, as part of the “War on Poverty,” the federal government created the Office of Economic Opportunity (OEO) to distribute federal funds to finance civil legal services for the poor.<sup>81</sup> The effect was enormous. In the first two years, 300 legal aid societies received federal funding that amounted to eight times the total amount received by legal aid societies in 1965.<sup>82</sup> In the same time period, “800 new law offices and almost 2000 new lawyers were funded [by the OEO].”<sup>83</sup> By 1971, the offices funded by the OEO processed 1,237,275 cases, up from 426,457 in 1965.<sup>84</sup>

The greatest impact of the early OEO funded programs was on larger causes. OEO funded programs initiated litigation to reform laws and institutions that affected underrepresented groups of people. Indeed, over the course of the first decade, several OEO-funded societies “won significant victories, largely in reforming and expanding federal entitlement programs,” including the expansion

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75. Scott L. Cummings, *The Politics of Pro Bono*, 52 UCLA L. REV. 1, 11 (2004).

76. *Id.* at 11–12.

77. *Id.* at 11.

78. *Id.* at 13.

79. MARTHA F. DAVIS, BRUTAL NEED: LAWYERS AND THE WELFARE RIGHTS MOVEMENT, 1960–1973, at 19 (1993).

80. Alan W. Houseman, *Legal Aid History*, in POVERTY LAW MANUAL FOR THE NEW LAWYER 18, 18 (Nat’l Ctr. on Poverty Law ed., 2002).

81. Cynthia Adcock, *Shaped by Educational, Professional, and Social Crises: The History of Law Student Pro Bono Service*, in PRIVATE LAWYERS AND THE PUBLIC INTEREST 25, 31 (Robert Granfield & Lynn Mather eds., 2009).

82. EARL JOHNSON, JR., JUSTICE AND REFORM: THE FORMATIVE YEARS OF THE OEO LEGAL SERVICES PROGRAM 71 (1974).

83. *Id.*

84. *Id.*

of welfare benefits, the adoption of state minimum wage hours for farm workers, and the expansion of food stamp and school lunch programs.<sup>85</sup>

But shifts in the political climate in the 1970s caused the federal government to limit its largesse. Major legal victories for OEO-funded legal societies against the government caused some politicians to question “why the government was paying lawyers to sue it.”<sup>86</sup> In an effort to undermine the viability and success of legal aid societies, President Richard Nixon created the Legal Services Corporation (LSC), an independent organization that received federal money that was to be distributed to local civil legal aid societies.<sup>87</sup> First, Nixon decreased funding to LSC. In 1982, politicians slashed LSC’s budget to \$241 million, down from \$680 million just two years earlier,<sup>88</sup> with a concurrent decline of twenty-five percent of legal services offices nationwide.<sup>89</sup> Today, state and local governments contribute nearly as much as LSC does to groups that advance civil legal services.<sup>90</sup> But the combined contribution of \$535 million still lags behind the \$680 million of thirty years ago.<sup>91</sup>

Next, Nixon and Congress passed rules, many of which are still in effect today, that limited how government money could be used by the civil legal aid societies. Today, civil legal aid societies that receive funds from LSC may not, among other activities, engage in class action litigation, engage in litigation that affects issues before Congress, or represent clients with welfare claims.<sup>92</sup> The new rules have effectively crippled the efforts of civil legal aid societies to effect broader change.<sup>93</sup>

The rules passed by Nixon and Congress also limited the individuals whom legal aid societies may help. Groups that receive LSC funds may not provide legal services to prisoners, undocumented aliens, or anyone with an income above 125% of the poverty level.<sup>94</sup> Nor may LSC-funded groups use federal funds to litigate cases that might generate fees if the case had been litigated by a private lawyer.<sup>95</sup>

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85. Cummings, *supra* note 75, at 20–21.

86. Adcock, *supra* note 81, at 25, 36.

87. *Id.*; Cummings, *supra* note 75, at 21–22; Deborah L. Rhode, *Whatever Happened to Access to Justice?*, 42 LOY. L.A. L. REV. 869, 880–81 (2009).

88. Adcock, *supra* note 81, at 36; Cummings, *supra* note 75, at 20.

89. Adcock, *supra* note 81, at 36.

90. Cummings, *supra* note 75, at 23.

91. *Id.*

92. 45 C.F.R. §§ 1612.3, 1612.9, 1639.3 (2014).

93. Cummings, *supra* note 65, at 524–26.

94. 45 C.F.R. §§ 1611.3, 1626.3, 1637.3; Douglas J. Besharov & Paul N. Tramontozzi, *Appendix A: Background Information on the Legal Services Corporation*, in LEGAL SERVICES FOR THE POOR: TIME FOR REFORM 209, 215 (Douglas J. Besharov ed., 1990); Rhode, *supra* note 87, at 880; Sandefur, *supra* note 25, at 81 n.4.

95. 45 C.F.R. § 1609.2.

Since the Nixon-imposed cuts, civil legal aid societies have focused on providing basic legal services to low-income clients. In 2011, 135 civil legal aid societies that received LSC funding saw a total of 899,817 cases that fell into ten broad categories: consumer, education, employment, family, health, housing, income maintenance, individual rights, juvenile, and miscellaneous.<sup>96</sup> The majority of those cases—over sixty percent—involved family matters (including adoption, child support, custody, divorce, and other family issues) and housing disputes (with the vast majority of housing disputes traditionally focused on landlord-tenant issues).<sup>97</sup>

While a portion of the low-income population receives help from civil legal aid societies, the restrictions attached to funding have left a number of people and legal causes outside the realm of what can be accomplished by civil legal aid societies. Restrictions placed on funding mean that only seventeen percent of the population qualifies for services from legal aid societies that receive money from LSC.<sup>98</sup> And for every 14,000 people who qualify for civil legal aid under LSC, only one full-time equivalent attorney exists.<sup>99</sup> When the pool is expanded to include attorneys who work for non-LSC funded civil legal aid groups and eligible clients, the number drops to one attorney for every 7000 eligible people.<sup>100</sup> A recent study suggests that the current civil legal aid system meets less than one-fifth of the needs of low-income people.<sup>101</sup> Those who do qualify for legal assistance must choose from societies that provide specialized services, “including homeless assistance, family law, eviction defense, debt collection defense, guardianships, and home equity fraud.”<sup>102</sup>

## 2. *Law School Clinics*

At roughly the same time that civil legal aid societies took shape in the early twentieth century, law schools began developing live-client legal clinics that served the poor. Beginning with the University of Pennsylvania and followed by Harvard Law School and George Washington University, universities established legal aid societies in an effort “to help members of the community who are too poor to hire a regular attorney in those cases where they need a lawyer’s services, and, second, to give students the practical education that comes from the experience of handling real cases.”<sup>103</sup> Later, in the 1960s, at the same time that the OEO granted money to community-based legal aid societies, twenty-nine of the eighty-six

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96. LSC Spreadsheet: CSR 2011 by CASE TYPE (on file with author).

97. Besharov & Tramontozzi, *supra* note 94, at 219–20.

98. Sandefur, *supra* note 25, at 95.

99. *Id.* at 83 (providing that in 1997, LSC funded the salaries of 3494 full-time equivalent lawyers to service the population of low income clients eligible for LSC-funded services).

100. *Id.* at 84.

101. Cummings & Rhode, *supra* note 25, at 2367.

102. Cummings, *supra* note 75, at 43.

103. Adcock, *supra* note 81, at 28.

university-based legal clinics received funding from the OEO.<sup>104</sup> In addition to the OEO money, at the same time nineteen law schools received over \$800,000 from the Council on Legal Clinics, a private foundation significantly funded from the Ford Foundation.<sup>105</sup> This money was to be used to fund poverty law clinics and “to discover and lay out new and better methods of educating law students about their future role as members of a profession.”<sup>106</sup>

Today, law school legal clinics provide a nominal amount of legal service to members of the community. Through over 809 legal clinics at 131 law schools, supervised law students provide legal services free of charge to people with general civil litigation needs, as well as in the areas of community economic development, immigration, and children and the law.<sup>107</sup> But the combined efforts of law students and supervising attorneys are the equivalent of 788 full-time lawyers each year.<sup>108</sup> Despite the impact that live-client legal clinics have on many individuals’ lives, the overall effect of the clinics on demand for legal services from the poor is low.

### 3. *Law Firm Pro Bono Programs*

Since the 1980s, pro bono programs at large and small law firms have evolved to help fill the gap left by civil legal aid societies. Efforts to provide legal services to the poor pro bono—an arrangement through which lawyers donate time and firm resources to litigate a claim for a party—began to take shape in the 1970s and quickly evolved during the 1980s for various reasons, such as efforts by the bar to encourage lawyers to help fill the gap caused by the limitation on LSC funding,<sup>109</sup> law firms’ use of pro bono to attract graduates from top law schools,<sup>110</sup> *American Lawyer*’s ranking of law firms based on their pro bono activities,<sup>111</sup> and professional model rules that encouraged lawyers to engage in pro bono.<sup>112</sup>

The type of cases pro bono attorneys litigate depends on the size of the firm in which the attorney practices. Lawyers at small law firms of between two and five attorneys—which comprise sixty percent of all lawyers in private practice—provide free or reduced fee representation to low-income clients that supplements

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104. *Id.* at 31.

105. *Id.*

106. *Id.*

107. Cummings, *supra* note 65, at 529.

108. *Id.* at 530 n.79.

109. Leslie C. Levin, *Pro Bono and Low Bono in the Solo and Small Law Firm Context*, in PRIVATE LAWYERS AND THE PUBLIC INTEREST, *supra* note 81, at 155, 157.

110. Cummings, *supra* note 75, at 35; Cummings & Rhode, *supra* note 25, at 2370.

111. Cummings & Rhode, *supra* note 25, at 2371.

112. MODEL RULES OF PROF’L CONDUCT R. 6.1.



services offered by other civil legal aid societies.<sup>113</sup> This includes help with divorce cases, personal bankruptcy, and similar small cases. One study has shown, however, that a large portion of the pro bono work conducted by solo and small firms is not given to the poor, but is given to friends and family, or the lawyer will report work done for clients who failed to pay a bill as pro bono.<sup>114</sup>

Larger law firms, which have greater man power and resources to devote to cases, often take on large-scale, reform-oriented cases that focus on a legal cause rather than an individual's legal claim. These cases tend to be the cases that LSC-funded organizations are barred from pursuing and that smaller public private firms or small practitioners cannot take on because of resource limitations.<sup>115</sup> A recent study found that large firm pro bono efforts tended to focus on cases involving immigration issues, civil liberties, voting rights, children/youth issues, and environmental issues.<sup>116</sup> To further the cause-based model of pro bono, firms have "signature projects" that "are designed to coordinate firm resources around a well-defined goal, create synergies between different practice groups, and build institutional knowledge and resources."<sup>117</sup> For example, Latham & Watkins sponsors a firm-wide initiative to help "unaccompanied refugee children detained by the government."<sup>118</sup> Likewise, Heller Ehrman White & McAuliffe provides assistance to individuals with legal complications arising from HIV/AIDS.<sup>119</sup>

But much like civil legal aid societies, many pro bono lawyers are institutionally constrained in the types of cases they can pursue. On one end of the spectrum of potential pro bono clients, some large firms will shy away from taking small claims or basic individual claims. One reason for this strategy is that large firms engaged in pro bono want to concentrate efforts on large-scale impact litigation out of a desire to capitalize on the greater resources of the firm. Another reason is because law firms want to create "positive public relations."<sup>120</sup> Firms engage in pro bono so that the firm can generate goodwill and good press by showing the impact that its assistance has on a population. A potential victory for an individual with a small claim will not generate the type of press that a victory for a larger cause would. That said, some firms have enacted clinic-based pro bono programs that attend to the basic legal needs of members of the community: domestic violence, wage-and-hour law, and landlord-tenant law.<sup>121</sup> Firms advertise to the community that they will hold a clinic at a specific location on a certain day

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113. Levin, *supra* note 109, at 166–68.

114. *Id.* at 165–68.

115. Scott L. Cummings & Ann Southworth, *Between Profit and Principle: The Private Public Interest Firm*, in PRIVATE LAWYERS AND THE PUBLIC INTEREST, *supra* note 81, at 183, 198–99.

116. Cummings, *supra* note 65, at 539.

117. Cummings, *supra* note 75, at 72–73.

118. *Id.* at 73.

119. *Id.*

120. *Id.* at 123.

121. *Id.* at 74–75.

or firm lawyers will staff social services offices on certain days.<sup>122</sup> Such representation, however, reaches a limited audience. Firms that host clinics do so for limited hours on limited occasions; lawyers who visit social service offices are only able to help the clients that happen to be present when they are there.<sup>123</sup> Neither of these groups of people have any promise of legal help after the initial meeting.

At the other end of the spectrum, firms must not accept large scale cases that might conflict with the regular business of the firm. Large firms generally represent corporate clients that are sued for an array of alleged offenses, including environmental damages, labor disputes, and consumer complaints. Because of the importance of these corporate clients to the firm's bottom line, firms generally refrain from pursuing claims pro bono that might conflict with the interests of current or future clients.<sup>124</sup>

#### 4. *Private Public Interest Law Firms*

Private firms that specialize in public interest law supplement the efforts of pro bono and civil legal aid societies.<sup>125</sup> Generally, these firms "are oriented toward the enforcement and reform of laws and institutions that affect broad social groups."<sup>126</sup> This includes law as diverse as employment discrimination and basic human rights claims. Unlike civil legal aid societies, these firms do not receive funding from LSC or other governmental agencies that might limit what types of cases they can pursue. And unlike law firms that prioritize the interests of paying clients over pro bono clients, these firms rarely have to worry about potential client conflicts, so the firm can pursue large-scale impact litigation against corporations.<sup>127</sup> This lack of restriction allows these firms to finance cases that "advance a vision of the public interest that enhances legal and political access for underrepresented groups or pursues a social change agenda that challenges corporate or governmental power."<sup>128</sup>

Unlike other for-profit law firms, private public interest law firms are not driven solely by profit. Indeed, "the 'return' [private public interest law firms] ultimately seek[] to maximize transcends economic profit."<sup>129</sup> Instead, the "raison

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122. *Id.* at 76.

123. *Id.* at 74–75.

124. Cummings, *supra* note 75, at 116–21; Rebecca L. Sandefur, *Lawyers' Pro Bono Service and Market-Reliant Legal Aid*, in PRIVATE LAWYERS AND THE PUBLIC INTEREST, *supra* note 81, at 95, 103.

125. *See generally* Cummings & Southworth, *supra* note 115, at 192–94.

126. Cummings, *supra* note 65, at 524.

127. Unlike corporate law firms that represent corporations, since private public interest law firms typically only represent individuals and classes of individuals, they do not have to worry about conflicts of interest.

128. Cummings, *supra* note 74, at 10.

129. *Id.* at 58.

d'être" of this type of firm is to pursue the "righteous case"—the case that would have great social impact, that would "right a manifest wrong,"<sup>130</sup> and that "presents a compelling injustice."<sup>131</sup> This includes cases that challenge broad education initiatives and requirements, cases that force multinational corporations to improve working conditions in factories, and cases that expose the human rights abuses of oil companies.<sup>132</sup>

But litigating large-scale cases against corporations or governments is not cheap.<sup>133</sup> While other for-profit law firms reinvest profits to finance future litigation,<sup>134</sup> many cases litigated by private public interest law firms fail to generate profits. Some well-established private public interest law firms might have lines of credit that they can draw on to cover expenses,<sup>135</sup> but other firms must self-finance much of their case load.

To accomplish this, these firms have developed a portfolio model of litigating a set of cases with a double bottom line that balances social impact and generating fees. The firm will litigate low-risk cases that, if won, have a nominal social reward, but will generate fees for the firm either through monetary reward against the defendant or through money gained through fee-shifting statutes or private attorneys general fee provisions.<sup>136</sup> Fee generating cases are still those that advance the core values of public interest law and generate "positive externalities"; these cases include employment discrimination, whistleblower antidiscrimination, and wage-and-hour laws.<sup>137</sup> Money generated from these cases will finance the high-risk, high socially rewarding cases—the righteous cases. Sometimes these cases will generate massive fees for the firm,<sup>138</sup> which can then be reinvested in future litigation. Other times, these cases generate no fees, only returning a social reward, or the case will be a loser.

The importance of litigating the righteous case causes the private public interest law firm to miss helping many people. Cases are only taken by the firms if they will further the broader social purpose of the firm. But even if a case might further that broader purpose, a firm may decline it because any judgment or settlement would yield a small amount of fees. For example, private public interest law firms accept some employment discrimination cases or whistle-blower cases,

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130. *Id.* at 63.

131. *Id.*

132. *Id.* at 21, 63.

133. *Id.* at 67 (citing an international human rights case, where most of the witnesses and conduct took place in Africa, "lasted for over five years, had totaled 'hundreds and hundreds and hundreds of thousands in costs . . . hundreds and hundreds and hundreds and hundreds'" (ellipsis in original) (citation omitted)).

134. KRITZER, *supra* note 6, at 12–13.

135. Cummings, *supra* note 74, at 29, 50–51, 66–67; Yeazell, *supra* note 24, at 186–98.

136. Cummings, *supra* note 74, at 12; Cummings & Southworth, *supra* note 115, at 190; Sandefur, *supra* note 25, at 81.

137. Cummings, *supra* note 74, at 58.

138. *Id.* at 63–64.

but they do so only if the monetary return on the time invested in those cases will be high. A partner at one private public interest law firm said that it only pursues such cases if the case will generate \$400,000 or more in fees.<sup>139</sup> Cases that would generate lower fees are declined so that the firm's resources can be directed at efforts that will more efficiently further a righteous case. This keeps the firm from pursuing many cases that either fail to meet the value driven purpose of the firm or fail to generate the money the firm needs that will allow it to litigate the types of cases that further the values of the firm.

As this section explored, the cause model of TPLF serves a diverse market, segmented by the institutional constraints placed on the financiers. While many people benefit from the provision of free legal services, many are left out. Pro bono programs provide litigation finance to many legal causes (environmental protection, immigration reform), but the focus on creating the greatest legal change comes at the expense of helping individuals with their basic legal claims. Private public interest law firms will litigate some of those basic claims (employment discrimination), but only if they provide a great-enough monetary reward. Civil legal aid societies provide help to members of the community with a wide variety of claims that neither pro bono programs nor private public interest law firms will pursue. But these legal aid societies are limited in their resources and turn down many cases. Who will take these rejected cases?

### B. *The Profit Model*

For the plaintiffs who fall outside of the support system provided by groups in the cause model, contingency fee lawyers exist to pursue their claim. Contingency fee lawyers, the only group under the profit model of TPLF, pursue cases for litigants and finance the litigation expenses, including the cost of expert witnesses, bond requirements (for medical malpractice cases), court filing fees, and the lawyer's time. Unlike financiers under the cause model, contingency fee lawyers typically operate with a single bottom line: generating a profit. In exchange for financing the claim, the lawyer receives a portion of any court-awarded remedy or settlement between the two litigating parties. This desire to generate a profit means that contingency fee lawyers typically take only cases that will result in a monetary award for the plaintiff; this includes all types of cases from social security to automobile accident cases, up to medical malpractice and product liability.

Contingency fee lawyers, however, cannot take every case that offers a possible profit. Cash flow limits the number of cases a contingency fee lawyer can pursue.<sup>140</sup> Cases like medical malpractice and commercial claims tend to be the

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139. *Id.* at 64.

140. KRITZER, *supra* note 6, at 97; Kritzer, *supra* note 5, at 303.

most profitable cases for a plaintiffs' attorney.<sup>141</sup> These types of cases, however, also tend to be the most expensive to litigate; they require expert witnesses, bonding, as well as the normal fees associated with litigating a case.<sup>142</sup> As one plaintiffs' attorney in Texas commented, medical malpractice cases "are way too technical . . . Easily you can spend \$100,000 without blinking . . . and we don't have that kind of cash laying around."<sup>143</sup> But while large firms can draw down a line of credit to cover those up-front expenses, many contingency fee lawyers lack such an arrangement.

To fund these cases, most contingency fee lawyers maintain a portfolio of cases including expensive, large-fee cases and inexpensive, low-fee cases. To fund the high-risk, labor-intensive, profit-generating cases, contingency fee lawyers litigate a larger number of low-risk, low-reward cases—workman's compensation, personal injury, or social security. These cases generate the fees that provide firms with a cash flow to "keep the lights on"<sup>144</sup>—or pay the firm's fixed costs—and leave a "reasonable profit."<sup>145</sup> Contingency fee attorneys then use the profit generated from these cases to finance a smaller number of more expensive, higher reward cases that generate the bulk of the firm's profits.<sup>146</sup> Indeed, the cash flow from the low-risk, low-reward cases is crucial in financing the higher risk cases; "[w]ithout cash flow coming in you can't pay your bills and you can't fund your cases."<sup>147</sup>

But even with the portfolio model, contingency fee lawyers cannot litigate all of the cases that fall through the cracks of the cause model. Surveys of lawyers in Texas and Wisconsin indicate that contingency fee lawyers turn away potential clients for a number of reasons. In Wisconsin, respondents suggested that they turn away at least half of the cases they are asked to take.<sup>148</sup> While some of these cases were denied on their merits, others were denied because the costs were too high.<sup>149</sup> A similar survey of plaintiffs' attorneys in Texas found that attorneys decline to take cases because of an inability to "front the costs" of litigation for expensive cases like medical malpractice and commercial litigation; "the process of taking a case to court is getting enormously expensive."<sup>150</sup>

What, then, happens to the potential plaintiffs who cannot afford to litigate a

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141. KRITZER, *supra* note 6, at 13; Kritzer, *supra* note 5, at 273.

142. Stephen Daniels & Joanne Martin, *It Was the Best of Times, It Was the Worst of Times: The Precarious Nature of Plaintiffs' Practice in Texas*, 80 TEX. L. REV. 1781, 1798 (2002).

143. *Id.*

144. *Id.* at 1783.

145. KRITZER, *supra* note 6, at 13; Daniels & Martin, *supra* note 142, at 1800 (finding that workman's compensation cases "provided a regular source of income that covered a small practice's overhead").

146. KRITZER, *supra* note 6, at 97.

147. Daniels & Martin, *supra* note 142, at 1782.

148. KRITZER, *supra* note 6, at 71.

149. *Id.* at 73–88.

150. Daniels & Martin, *supra* note 142, at 1812.

claim on their own and who are unable to receive litigation finance because their case fails to appeal to any of the other groups?

### III. GETTING MORE THIRD PARTIES TO PAY FOR COURT

Until recently, cash-strapped contingency fee lawyers have had few options to increase cash flow so as to take on more clients. In the last six years, however, hedge funds, private equity groups, and banks have started investing in litigation, giving plaintiffs and law firms cash in exchange for a piece of any settlement or award.<sup>151</sup> The practice is niche, with less than a dozen firms investing over \$1 billion annually in specific types of claims.<sup>152</sup> While the practice is booming, contingency fee lawyers and their clients have received little, if any, of the investments.

Making litigation finance available to contingency fee lawyers could dramatically increase access to justice. As discussed in Part II of this Note, contingency fee lawyers often handle the cases that other third-party litigation financiers refuse to litigate. By providing contingency fee lawyers with cash through investments, those lawyers would be able to litigate a larger number of cases and thus serve a broader group of potential litigants. For the plaintiffs that have been adversely affected by the heightened pleading standards of *Iqbal* and *Twombly*, these new investors could provide attorneys the cash flow necessary for the attorney to engage in effective pre-filing investigations that would enable a complaint to survive a Rule 12(b)(6) motion to dismiss. For the plaintiffs that have other claims that are expensive to litigate, like medical malpractice, the loans could provide the attorney with the cash necessary to hire expert witnesses or conduct more expansive discovery.

This part will describe the financing schemes available to contingency fee lawyers and their clients as well as to large law firms and their clients. Contingency fee lawyers and their clients have traditionally been limited to loans. But evidence suggests that, in the wake of the recession, interest rates on those loans have skyrocketed, making it too expensive for contingency fee lawyers to use the loans.<sup>153</sup> Large law firms, on the other hand, have benefited from lines of credit with major banks. Recently, large law firms and their clients have additionally benefited from access to investment financing from hedge funds, private equity firms, and traditional banks. As this section will argue, due to the current market structure of litigation finance, contingency fee lawyers will likely soon benefit from greater access to the same litigation finance currently only available to large law firms and

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151. See *infra* Part III.B.

152. See *infra* Part III.B.

153. See *infra* Part III.B.3.

law firm clients. As contingency fee lawyers receive more cash, litigants who have been locked out of the courtroom might gain greater access to justice.

#### A. Existing Modes of Finance

For contingency fee lawyers that lack enough cash to litigate claims, options to get more cash have been limited. Today, simple Internet searches reveal the number of banks and lenders that are willing to extend money to lawyers and law firms. But because of the private nature of the banks and the lawyers who accept the loans, no information is available about the pervasiveness of the practice. Anecdotal evidence suggests that some contingency fee lawyers have welcomed the cash. A Manhattan lawyer recently borrowed \$45,000 from a litigation lending company, Ardec Funding, in June 2010 to help litigate a medical malpractice suit.<sup>154</sup> The attorney used the money to hire several expert witnesses, including two doctors and an economist.<sup>155</sup> Yet other evidence, such as the large numbers of lawyers that claim they have to turn down cases because of a lack of cash flow, as discussed in Part II of this Note, suggests that the practice is rare.

Other end-around methods exist for contingency fee lawyers to receive money that could help litigate a case. Lenders in many states lend money directly to plaintiffs against any potential settlement or judgment.<sup>156</sup> Called “consumer legal funding,” this practice has been available since as early as the 1980s.<sup>157</sup> The loans advanced by the lenders presettlement or prejudgment operate similarly to loans advanced to lawyers: they are nonrecourse—if there is a judgment in the defendant’s favor, the plaintiff owes the lender nothing. Available evidence suggests, however, that these loans complement rather than supplement the contingency fee contract. Rather than using the money to further litigation efforts, plaintiffs use the money advanced to cover living expenses and doctors’ bills that accrue during trial or while the plaintiff is waiting to receive cash from a judgment or settlement.<sup>158</sup>

#### B. New Models of Finance

Recently, a new class of investors have entered the market to offer plaintiffs and lawyers money for a share of any settlement or judgment. Like the loans previously discussed, the investments are nonrecourse—if the plaintiff loses the

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154. Binyamin Appelbaum, *Putting Money on Lawsuits, Investors Share in the Payouts*, N.Y. TIMES, Nov. 15, 2010, at A1.

155. *Id.*

156. Barksdale, *supra* note 20, at 707–08; Billy Shields, *Taken for a Ride?: Litigation Finance Companies Say They Provide an Important Service, but Critics Say They Take Advantage of Desperate Victims*, MIAMI DAILY BUS. REV., May 12, 2008, at A6; Christine Simmons, *Client Sues Firm After Funders Recover Most of His Settlement*, N.Y. L.J., July 19, 2012, at 1.

157. GARBER, *supra* note 16, at 9; Steinitz, *supra* note 20, at 459–60.

158. See Shields, *supra* note 156; Simmons, *supra* note 156, at 1; A.B.A. Comm’n on Ethics 20/20, *supra* note 20, at 6.

case, neither she nor her attorney are responsible for repaying the initial investment. But the investments are far larger than the loans. Burford Capital, one of the first investment groups to enter the market, typically invests between \$3 and \$5 million dollars in a case and receives an agreed-upon percentage of the award or settlement, which can vary between ten and forty-five percent.<sup>159</sup>

Investors have poured billions into litigation investments. As of 2010, at least six investment firms offer TPLF,<sup>160</sup> with over a billion dollars invested each year.<sup>161</sup> Several of the funds boast assets of hundreds of millions. Juridica Capital Management raised \$180 million during initial public offerings on the London Stock Exchange, and Burford Capital had \$300 million in capital for litigation investment as of 2012.<sup>162</sup> And investors continue to enter the market;<sup>163</sup> a Chicago-based fund backed by \$100 million announced initial investment efforts in April 2013,<sup>164</sup> and an Irvine-based fund opened a month earlier.<sup>165</sup>

With so few investors engaged in litigation finance, litigation financiers can be picky. Although the firms engaged in litigation finance have hundreds of millions of dollars each to invest, the firms make few investments. Burford invested in only thirty-five cases over two years.<sup>166</sup> As of 2013, Juridica Investments had only made twenty-four investments since 2007.<sup>167</sup>

And the few investments that the firms do make go to high-reward, low-risk commercial cases that produce massive profits. While pro bono programs or private public interest lawyers might take claims that challenge legal precepts, the new litigation financiers only invest in cases that have the chance “to produce a substantial return.”<sup>168</sup> The financiers specifically target cases where returns can be greatest by finding cases that are unlikely to be appealed, where the other side has

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159. Lawrence S. Schaner & Thomas G. Appleman, *Third-Party Litigation Funding in the United States*, 32 REVISTA DE ARBITRAGEM E MEDIAÇÃO 175, 178 (2012).

160. GARBER, *supra* note 16, at 14.

161. N.Y.C. BAR, FORMAL OP. 2011-2, THIRD-PARTY LITIGATION FINANCING 1 (2014); Steven R. Strahler, *Chicago Company Seeks to Profit from Lawsuits*, CRAIN'S CHI. BUS. (Apr. 8, 2013), <http://www.chicagobusiness.com/article/20130408/NEWS01/130409842/chicago-company-seeks-to-profit-from-lawsuits>.

162. Richard Lloyd, *The New, New Thing: Two Publicly Listed Funds Are Investing in Early-Stage Commercial Litigation. Is This the Start of a Revolution, or a Sideshow for a Few Former Am Law 100 Lawyers?*, AM. LAW., May 17, 2010; McDonald, *supra* note 16.

163. Michael J. de la Merced, *Firm Focused on Investing in Lawsuits Brings in Old Leader*, N.Y. TIMES DEALBOOK (Jan. 23, 2013, 4:21 PM), <http://dealbook.nytimes.com/2013/01/23/firm-focused-on-investing-in-lawsuits-brings-in-old-leader/>.

164. William Alden, *New Firm Plans to Invest in Lawsuits*, N.Y. TIMES DEALBOOK (Apr. 8, 2013, 7:24 AM), <http://dealbook.nytimes.com/2013/04/08/new-firm-plans-to-invest-in-lawsuits/>.

165. Casey Sullivan, *Former Prosecutor Stolper Starts Litigation Finance Firm*, REUTERS (Mar. 13, 2013, 3:46 AM), <http://www.reuters.com/article/2013/03/13/us-usa-stolpernorell-idUSBRE92C07820130313>.

166. McDonald, *supra* note 16.

167. JURIDICA INVS., LTD., ANNUAL REPORT & ACCOUNTS 2012, at 6, available at [http://www.juridicainvestments.com/~media/Files/J/Juridica/Annual%20Reports/reports/ar-2012.pdf](http://www.juridicainvestments.com/~/media/Files/J/Juridica/Annual%20Reports/reports/ar-2012.pdf).

168. Jonathan D. Glater, *Investing in a Portfolio of Lawsuits*, N.Y. TIMES, June 3, 2009, at B8.



deep pockets to pay any judgment or settlement, or where liability has already been admitted.<sup>169</sup> These tend to be antitrust, patent infringement, or commercial claims. The scheme is paying off. Burford Capital, one of the first groups organized that invests in commercial litigation, had a ninety-one percent return on its investment in 2011.<sup>170</sup>

### 1. *Law Firms As Beneficiaries*

Large law firms are one of the beneficiaries of the new investors. Shifts in the dynamics of the business of law have caused many law firms to seek out investments. Traditionally, large law firms billed clients during the course of litigation; the receipt of money from clients during litigation was then used to pay the firm's fixed costs, as well as to fund the ongoing litigation efforts. In the event that a firm had a decreased cash flow, a firm could draw down a line of credit extended from a commercial bank.<sup>171</sup> During the most recent recession, in reaction to excessive borrowing by some law firms, large banks decreased or eliminated lines of credit to law firms, leaving the firms without cash in times of need.<sup>172</sup> Also as a result of the recession, some cost-conscious law firm clients have requested that firms offer alternative fee arrangements.<sup>173</sup> In these arrangements, the firm may structure a hybrid fee arrangement with its business client, whereby the firm charges a lower hourly rate in the expectation of receiving a bonus upon favorable settlement or judgment.<sup>174</sup> To replace the cash once received from banks and to supplement cash lost upfront because of the alternative fee arrangements, several law firms have received case-by-case litigation investment from a litigation financier in exchange for a portion of the damages or settlement.<sup>175</sup> Juridica Capital Management, for example, places sixty percent of its active investments with AmLaw 200 firms.<sup>176</sup> Burford Capital similarly invests mostly in litigation handled by large law firms, with the typical investment ranging from \$3 to \$15 million.<sup>177</sup> An array of law firms have received the money, including Simpson Thacher & Bartlett, Latham & Watkins, and Patton Boggs.<sup>178</sup>

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169. See Lloyd, *supra* note 162.

170. Alden, *supra* note 16, at B3.

171. See, e.g., *Legal Specialty Group*, WELLS FARGO, <https://www.wellsfargo.com/the-private-bank/solutions/private-banking/legal-specialty-group/> (last visited Mar. 18, 2015).

172. Jacqueline Palank, *Law Firms Are No Longer Seen as a Safe Bet for Lenders*, WALL ST. J.L. BLOG (Apr. 30, 2012, 9:06 AM), <http://blogs.wsj.com/law/2012/04/30/law-firms-are-no-longer-seen-as-a-safe-bet-for-lenders/>.

173. Jonathan D. Glater, *Billable Hours Giving Ground at Law Firms*, N.Y. TIMES, Jan. 30, 2009, at A1.

174. Molot, *supra* note 20, at 100; Steinitz, *supra* note 18, at 1329.

175. Glater, *supra* note 168.

176. Lloyd, *supra* note 162.

177. Schaner & Appleman, *supra* note 159, at 178; McDonald, *supra* note 16; Nate Raymond, *Sean Coffey Launches New Litigation Finance Firm with Juridica Cofounder*, AMLAW DAILY (June 20, 2011, 6:20 PM), <http://amlawdaily.typepad.com/amlawdaily/2011/06/seancoffeylitigationfund.html>.

178. Alden, *supra* note 16.

## 2. *Businesses As Beneficiaries*

Businesses that are party to litigation have also received funding from the new financiers.<sup>179</sup> In this situation, a corporate plaintiff that has a claim against another corporation will receive cash from a financier in exchange for a piece of the settlement or court award.<sup>180</sup> A litigant might choose this route for a number of reasons. The litigant might lack the cash necessary to pay lawyers that bill hourly through the end of trial. The litigant might need cash to hire a more experienced—and more expensive—law firm to litigate the matter. Or the corporate litigant might accept the cash for more strategic reasons. When a business receives litigation financing, it might signal to the defendant the plaintiff's belief in the quality of the claim and, in the process, gain the plaintiff a stronger bargaining position during settlement negotiations.<sup>181</sup>

## 3. *Contingency Fee Attorneys As Future Beneficiaries*

Contingency fee attorneys, like those discussed in Part II of this Note, have received only a small portion of the funding. Stephen Donzinger, a New York-based plaintiffs' attorney, received over \$8 million in investments from several litigation investors, including Burford Capital, while he represented thousands of Ecuadorians in their lawsuit against Chevron for environmental damages.<sup>182</sup> He used the money to hire environmental experts, attorneys in Ecuador, and eventually the Washington, D.C., firm Patton Boggs to aid in the litigation efforts.<sup>183</sup> With the help of the investments, the legal team Donzinger assembled achieved a \$19 billion judgment against Chevron.<sup>184</sup>

But available information on investment strategies indicates that Donzinger is an exception to the norm. Available evidence suggests that contingency fee lawyers receive a small share, if any, of investments.<sup>185</sup> Most of the firms that invest in litigation are privately held, which means they do not have to disclose their investment activity.<sup>186</sup> And many firms and businesses that seek litigation investments ask that their names not be disclosed.<sup>187</sup> But, Richard Fields, Chairman of the Board at Juridica, has noted that Juridica “won't invest in

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179. *Id.* The other forty percent of Juridica's investments go directly to the plaintiff-business. *Id.*

180. Steinitz, *supra* note 18, at 1276.

181. GARBER, *supra* note 16, at 15.

182. Steinitz, *supra* note 20, at 467–68.

183. Keefe, *supra* note 19, at 43–44.

184. Andrew Smith, *Chevron to Fight Multi-Billion Ecuador Ruling*, CNN MONEY (Feb. 15, 2011, 8:17 AM), [http://money.cnn.com/2011/02/15/news/international/chevron\\_amazon/index.htm](http://money.cnn.com/2011/02/15/news/international/chevron_amazon/index.htm).

185. *See* Kritzer, *supra* note 5, at 270–72; Schneyer, *supra* note 5, at 372 n.12.

186. *See* Lloyd *supra* note 162.

187. *See id.*; *see also* McDonald, *supra* note 16.

personal injury, mass torts, or class actions,” the types of cases typically handled by contingency fee lawyers.<sup>188</sup>

Contingency fee lawyers could soon receive litigation investment as the market for litigation investment evolves. On one side of the equation, more investors will continue to enter the market. While the annual investment in litigation is estimated at \$1 billion, approximately \$300 billion is spent on litigation each year;<sup>189</sup> the gap between the amount invested and amount spent on litigation represents the amount of opportunity for greater investment. Similarly, as the recession continues to wane, banks that stopped lending to law firms during the recession will likely reenter the market.<sup>190</sup> Those banks will likely lend money to law firms at lower effective equivalent interest rates than offered through litigation investment.

Other banks and large, traditional, institutional investors that have refrained from investing in litigation may, too, enter the market. Some commentators believe that these investors have remained out of litigation finance due to the negative stigma surrounding the practice.<sup>191</sup> The stigma likely derived from the practices of investors who often lent money to individual plaintiffs that were often involved in personal injury cases.<sup>192</sup> But as investment funds and reputable law firms continue to enter the litigation finance market, the negative stigma will likely decrease. As the stigma decreases, the traditional, institutional investors may enter the market as well.

As new investors enter the market, investors will have to seek out new investment opportunities. The hedge funds and private equity funds that continue to enter the market now do so because of the high profit margins available. And indeed, firms continue to enter the market. Through April 2013, two new investment firms have entered the market.<sup>193</sup> As more of these investors enter the market, the availability of high-stakes, low-risk commercial claims will eventually dry up. Some attorneys have already recognized this. Boston attorney Anthony M. Doniger recently said, “I don’t have a sense that there’s any burgeoning need” for litigation finance among large firms.<sup>194</sup> One recent article in a legal magazine has confirmed that investors have contacted smaller sized law firms: New England-based attorneys claim that they have received more solicitations for litigation finance recently.<sup>195</sup>

As investment strategies evolve and investors look for new opportunities,

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188. Lloyd, *supra* note 162.

189. AM. ARBITRATION ASSOC., DISPUTE-WISE BUSINESS MANAGEMENT 1 (2006), available at [https://www.adr.org/aaa/ShowPDF?doc=ADRSTG\\_004327](https://www.adr.org/aaa/ShowPDF?doc=ADRSTG_004327).

190. See Molot, *supra* note 20, at 96; Palank, *supra* note 172.

191. Molot, *supra* note 20, at 102.

192. Steinitz, *supra* note 18, at 1271–72.

193. See *supra* Part III.B.

194. McDonald, *supra* note 16.

195. *Id.*

contingency fee lawyers might start to receive investment opportunities for a few reasons. First, contingency fee lawyers and litigation financiers have perfectly aligned incentives. Contingency fee lawyers, much like litigation financiers, pursue cases that, if followed through to settlement or judgment, will produce an award that will yield a profit.

But, as discussed in Part II of this Note, contingency fee lawyers decline to litigate many potentially profitable cases each year simply because they lack the capital necessary to litigate the case. While some contingency fee lawyers may have access to loans, borrowing money is expensive and difficult to get. Banks have become more selective in their lending practices, evaluating firm financials more deeply and requiring personal guarantees on money advanced.<sup>196</sup> Then, when banks lend the money, it comes at great costs. Take the case mentioned above, where the attorney borrowed \$45,000 to fund a medical malpractice suit. While the jury found in favor of the plaintiffs and awarded damages of \$510,000, the attorney has had to pay \$900 a month in interest payments—annualized to a twenty-four percent interest rate—until the award is paid.<sup>197</sup> Such a great expense likely makes contingency fee lawyers reluctant to take out loans. While the loans provide access to cash to pay for litigation, the interest payments on the loans decrease the cash flow of the firm. Although the loan provided the cash necessary to pursue one case, the need to service the loan may prevent a firm from pursuing another case. But if contingency fee lawyers had access to cheaper financing, they could pursue more cases, generating more profits for both their firms and for the financiers.

Second, the new investors that will likely enter the market might have a taste for investments with lower capital commitments than those currently extended by financiers to large law firms and businesses. This desire for lower capital commitments might derive from investors' desire to invest in cases that require less capital or from investors' desire to make smaller investments in larger cases. Either way, the amount of money involved in cases litigated by contingency fee lawyers tends to be quite lower than the money involved in cases financed by the new third parties. Contingency fee lawyers in Texas reported receiving awards and settlements that approached \$750,000 dollars for medical malpractice cases;<sup>198</sup> employment discrimination cases reported by contingency fee lawyers in Los Angeles similarly reported judgments that reached several hundreds of thousands of dollars.<sup>199</sup> For awards that size, the amount of investment needed will likely be far less than currently offered by investors; an amount potentially attractive to new investors.

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196. Martin, *supra* note 20, at 72; Palank, *supra* note 172.

197. Appelbaum, *supra* note 154.

198. Daniels & Martin, *supra* note 142, at 1789.

199. Cummings, *supra* note 74, at 64.

#### 4. *Increased Access to Justice*

As discussed in Parts I and II of this Note, contingency fee attorneys must turn away potential client-plaintiffs because the attorney cannot afford to litigate what might be a meritorious claim. For some attorneys and clients, this problem has become more acute in the wake of *Iqbal* and *Twombly*. Critical facts to a case used to be unearthed during discovery, the costs of which were generally paid by the defendant. But changes in pleading rules now require plaintiffs to include those facts in their pleading.<sup>200</sup> This requires plaintiffs (or the plaintiffs' attorney) to pay for a pre-filing investigation to uncover those facts. As some plaintiffs (or their attorneys) are unable to pay for the investigation, some cases are never pleaded while others fail to survive a Rule 12(b)(6) motion to dismiss because the pleading lacked sufficient factual allegations.

But with easier access to financing, contingency fee lawyers will be able to help solve the access to justice problem exacerbated by *Iqbal* and *Twombly*. For claims most affected by the heightened pleading standards, contingency fee lawyers might best handle the FLSA claims, contract claims, and consumer credit claims because of the potential for a monetary settlement or judgment. With access to litigation finance, the contingency fee lawyer could help the above classes of plaintiffs gain access to justice in one of two ways. First, the attorney could simply engage in a pre-filing investigation that would uncover the facts necessary to survive a Rule 12(b)(6) motion to dismiss. The attorney might uncover the same facts during this investigation that she would have otherwise uncovered during discovery. While the pre-filing investigation will not guarantee a favorable outcome for the plaintiff, it increases the chances that the plaintiff will reach the same outcome that he would have under the *Conley* regime.

Second, by receiving litigation finance, the plaintiff's attorney sends a strong signal to the defendant about the strength of their case. Defendants and defense attorneys might understand that contingency fee lawyers that have cash will be able to engage not only in the pre-filing investigations, but also will be able to pour more resources into other phases of the trial. Such a signal might encourage defendants to settle cases early on in the litigation process.

The access to cash could further help other potential plaintiffs whose cases are typically handled by contingency fee lawyers. In the surveys of contingency fee attorneys in Wisconsin and Texas, discussed in Parts II and III of this Note, the attorneys noted that they are constrained in the number and types of cases they can pursue due to costs. Attorneys in both states stated that they must turn down high-reward cases, like medical malpractice, because they or their firm lack the cash needed to pay for the litigation expenses.<sup>201</sup>

Increasing access to justice through litigation finance seems possible. While

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200. Clermont & Yeazell, *supra* note 32, at 830.

201. KRITZER, *supra* note 6, at 13; Daniels & Martin, *supra* note 142, at 1798.

contingency fee lawyers can currently borrow money from lenders, the costs of borrowing are too high. But a further expansion of a new form of litigation finance could soon reach contingency fee lawyers. As the money reaches contingency fee lawyers, plaintiffs who cannot afford to litigate their own claim and lawyers who cannot afford to litigate the claim for them could soon see their day in court.

But, for this possibility to become a reality, legal regimes and professional rules need to be adopted or amended. Investing in litigation violates centuries-old laws concerning how lawsuits are brought to court. The argument can—and has—been made that this new form of TPLF is still illegal. But, as the final part of this Note will explore, states have started adopting or amending existing legal and regulatory regimes to allow for TPLF. But more needs to be done to ensure that the new financing scheme can benefit the greatest number of people. This Note will conclude with suggestions on what changes in rules need to be adopted or amended for this to happen.

#### IV. ALLOWING MORE THIRD PARTIES TO PAY FOR COURT

To allow for the meaningful expansion of TPLF, professional rules and legal regimes need to be changed or developed. Critics of the new form of litigation finance argue that the practice violates a constellation of ethical and professional rules; because of those conflicts, they argue that any expansion of TPLF should be banned. These critics also claim that the new form of litigation finance will cause a number of evils, including the filing of more frivolous litigation. But while the expansion of the new form of litigation finance comes into tension with certain rules or regulations, the benefits of the expansion, as addressed in Part III of this note, outweigh the potential costs. Because of the potential benefits, bar organizations and state and federal legislators should consider modifying or introducing new rules and regulations that will allow this new form of litigation finance to benefit those who need access to it to litigate their claims. This part of this Note will explore the various objections to the expansion of litigation finance, and at each step, suggest modifications to current rules or regulations, propose new regulations, and dispel certain claims critical of litigation finance.

##### A. *Champerty and Maintenance*

The legal status of this new form of TPLF is complicated. Traditionally, the common law proscribed such investing. During the Middle Ages in England, courts adopted rules that dated back to ancient Greece and Rome that prohibited one party from funding another party's lawsuit.<sup>202</sup> Laws against maintenance prohibited "assist[ing] a litigant in prosecuting or defending a lawsuit; [or]

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202. Max Radin, *Maintenance by Champerty*, 24 CALIF. L. REV. 48, 49–56 (1935).

meddl[ing] in someone else's litigation"<sup>203</sup> More specifically, laws against champerty, a type of maintenance, prohibited a person who is not party to a suit from funding the suit in exchange for a portion of the settlement or judgment.<sup>204</sup> In England, courts used the laws to prevent the landed gentry from funding lawsuits that belonged to a poor person.<sup>205</sup> The gentry used such lawsuits to diminish the power of rival land owners or to challenge the power of the courts.<sup>206</sup>

Some courts in the United States declined to adopt or enforce the rules through the common law. While many states acknowledge the common law doctrines of maintenance and champerty,<sup>207</sup> courts were loath to enforce the rules because they "had no real foundation in the United States."<sup>208</sup> The Supreme Court first declared the permissibility of contingency fees in the face of laws against maintenance in the 1877 case of *Stanton v. Embrey*.<sup>209</sup> There, the Court noted that "[t]he proposition (i.e. that contingent fees are legal) is one beyond legitimate controversy."<sup>210</sup> States, one-by-one, approved laws that exempted contingency fees from laws against maintenance, with Maine becoming the last state to approve the fees in 1965.<sup>211</sup> Courts similarly chose not to enforce laws against maintenance with regard to those who provided legal services to the poor.<sup>212</sup> The Supreme Court formally ruled in 1963 that civil legal aid societies could sue on behalf of others, under the protection of the First Amendment.<sup>213</sup>

Now, as more attorneys receive investment from third parties, many states have grappled with whether the laws against maintenance and champerty should be enforced or resurrected. Some states, like Massachusetts and South Carolina, have fully abandoned the rules against maintenance and champerty.<sup>214</sup> Indeed, one study conducted in 2010 found that twenty-eight states permit maintenance in its broadest form, with sixteen of those states explicitly permitting champerty.<sup>215</sup> Other states have taken a middle path. Legislators in Ohio and Maine have passed laws that permit champertous relationships, but require the financiers to register with state authorities.<sup>216</sup> And yet other states have ratcheted up laws that proscribe

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203. BLACK'S LAW DICTIONARY 1097 (10th ed. 2014).

204. *Id.* at 279.

205. Radin, *supra* note 202, at 61–64.

206. Steinitz, *supra* note 18, at 1287; Radin, *supra* note 202, at 61–64.

207. Radin, *supra* note 202, at 68.

208. *Id.*

209. *Stanton v. Embrey*, 93 U.S. 548 (1876).

210. Radin, *supra* note 202, at 71 n.84 (citing *Stanton*, 93 U.S. at 548).

211. Jeremy Kidd, *To Fund or Not to Fund: The Need for Second-Best Solutions to the Litigation Finance Dilemma*, 8 J.L. ECON. & POL'Y 613, 636 (2012).

212. Lyon, *supra* note 20, at 582.

213. *Id.*

214. Schaner & Appleman, *supra* note 159, at 183.

215. Anthony J. Sebok, *The Inauthentic Claim*, 64 VAND. L. REV. 61, 98–99 (2011).

216. Schaner & Appleman, *supra* note 159, at 179.

investing. Courts in Minnesota and Nevada, for example, have specifically stated that investing in lawsuits is champertous and, thus, illegal.<sup>217</sup>

### B. *Concerns over Increased Litigation*

Business leaders have also expressed concerns over the expansion of litigation finance. One criticism of the new form of TPLF is that giving potential plaintiffs and litigators more money will “permit[] [them] to offload risk” and encourage plaintiffs and attorneys to file more lawsuits, many of which would be frivolous.<sup>218</sup> Furthermore, the critics argue that the increased filing of lawsuits will strain an already overburdened civil legal system and increase the cost of business because of the need to defend the claims against them.<sup>219</sup>

These concerns, however, are slightly overblown. As previously discussed, the newest wave of litigation finance has not resulted in a massive number of lawsuits filed. Two of the six companies that have funded lawsuits have only invested in fifty-nine cases since 2007.<sup>220</sup> As TPLF evolves, and this Note suggests that it will, more lawsuits will inevitably be filed than would have been without litigation finance. Such has been the case in Australia, where the type of TPLF that is expanding in the United States has been legal in many jurisdictions since as early as 2006.<sup>221</sup> In a 2009 study by David Abrams and Daniel Chen, the two researchers found that the number of lawsuits filed in jurisdictions in Australia where litigation finance is legal had increased after litigation finance became legal.<sup>222</sup>

But more litigation does not necessarily equate to more frivolous litigation. Financiers have little incentive to fund frivolous lawsuits. Litigation financiers have an interest—and in the case of the publicly traded companies, a fiduciary duty—in maximizing returns on investment. If a financier believes a case to be meritless or a loser, the financier will not likely invest in the case due to the potential loss on investment. Nor would a lawyer likely litigate a case if he believes it to be a loser. Although litigation finance will allow him to offload a portion of the risk that he normally would have carried if he litigated the case on contingency, the lower level of risk in his portfolio does not necessarily mean that he will pursue riskier cases. Nor does it mean that the attorney, nor a financing company, would litigate a truly frivolous case.

More broadly, concerns that litigation finance might encourage more

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217. *Id.* at 182.

218. BEISNER ET AL., *supra* note 29, at 5.

219. *Id.* at 4–5.

220. *See supra* notes 166–167 and accompanying text.

221. *Campbell's Cash and Carry Pty. Ltd. v Fostif Pty. Ltd.* [2006] HCA 41 (Austl.); *see also* Dietsch, *supra* note 17, at 702–05; Michael Legg et al., *The Rise and Regulation of Litigation Funding in Australia*, 38 N. KY. L. REV. 625, 627–32 (2011).

222. Abrams & Chen, *supra* note 17, at 27.



litigation ignores the proposition that more litigation is not necessarily a bad outcome. Indeed, when litigation finance is provided to those who would pursue litigation but for the lack of capital, litigation finance helps those who have been locked out of the courtroom. As Parts I and II of this Note suggested, a large number of plaintiffs lack access to justice because either they or the contingency fee lawyers they hire cannot afford certain litigation expenses, like pretrial investigations, which would help them gain access to the courtroom. While providing these plaintiffs with the means to litigate their claims will necessarily cause more litigation, the right to sue over an injury, as noted in *Marbury v. Madison*, is “[t]he very essence of civil liberty.”<sup>223</sup> Indeed, the Supreme Court has repeatedly stated that “[o]ne of the first duties of government is to afford that protection”<sup>224</sup> and that Americans have a “fundamental constitutional right of access to the courts.”<sup>225</sup>

Furthermore, more litigation will benefit not only the individual who will be able to file a claim, but it will also benefit the legal system in general. In their research on Australia, Abrams and Chen compared a set of cases litigated with third-party finance to a set of cases that were funded without third-party finance.<sup>226</sup> The cases that were financed and reached a favorable outcome for the funded party were cited, on average, over twice as often as the cases that were unfunded.<sup>227</sup> This outcome suggests that cases that receive funding were not only meritorious, but they also created some procedural value by generating good law that has served as precedent for other cases.

### C. Concerns over Duty of Loyalty and Fiduciary Duty

Critics also express concern that inviting financiers to take part in litigation might compromise a constellation of written and unwritten professional rules. For one, critics fear that introducing a third party will compromise the attorney-client relationship by introducing a party into the relationship whose goals and duty are different than the attorney and the client.<sup>228</sup> The attorney is bound by the duty of loyalty to the client, which includes allowing the client to determine the course of litigation.<sup>229</sup> If the client decides that she would like to settle the case at any point—even if it is for an amount less than the attorney believes is possible—the attorney must abide by the client’s decision.<sup>230</sup> But, as critics argue, financiers owe

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223. *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 163 (1803).

224. *Id.*

225. *Bounds v. Smith*, 430 U.S. 817, 828 (1977).

226. See Abrams & Chen, *supra* note 17, at 41.

227. *Id.*

228. BEISNER ET AL., *supra* note 29, at 7–8.

229. MODEL RULES OF PROF'L CONDUCT R. 1.7 cmt. 1; see also Richard Wasserstrom, *Lawyers as Professionals: Some Moral Issues*, 5 HUM. RTS. 1, 15–24 (1975).

230. MODEL RULES OF PROF'L CONDUCT R. 1.2(a); see also Lynn Mather, *What Do Clients Want? What Do Lawyers Do?*, 52 EMORY L.J. 1065, 1082–85 (2003).

no such duty to the client.<sup>231</sup> Instead, they might owe a fiduciary duty to shareholders who want to maximize the return on the investment. Critics fear that, in an effort to secure funding, clients may “relinquish some decision-making authority to the funder.”<sup>232</sup> By giving the financier ultimate power, he will possibly litigate the case past settlement to a jury award in an effort to maximize the return on investment. In doing so, the purpose of the litigation will stray from making the plaintiff as whole as she would like to making the financier as whole as possible.

More recently, concerns have been raised about how the structure of investments might displace the client as the primary beneficiary of any settlement or award.<sup>233</sup> In cases where litigation finance has been provided to the attorney, it is unclear whether the financier’s stake in the settlement or reward is deducted from the attorney’s or client’s portion of the settlement or award. In a typical contingency fee contract between an attorney and the client, the attorney’s fee is calculated relative to the total settlement or award. Once the judgment is split between the attorney and the client, the attorney is also permitted to deduct from the client’s portion certain expenses incurred during the trial. The rules vary from state to state, but attorneys are generally permitted to further deduct expert witness fees, costs of investigation, and “other services properly chargeable to the enforcement of the claim or prosecution of the action.”<sup>234</sup> A judge in New York recently insinuated that clients may be responsible for paying the litigation finance company, but only if the clients are informed that they will be responsible for such costs.<sup>235</sup>

Another concern is who collects money from a settlement or judgment first—the clients, the attorney, or the financier? Because the firms that engage in litigation finance are typically privately held, and because the contracts signed between the financiers and the attorneys (and possibly with the clients) are not required in financial disclosures, little is known about how the agreements are typically structured. Recently, however, one controversial finance contract was made public. The contract was the heart of the litigation finance agreement between a group of Ecuadorians, represented by New York attorney Steven Donziger, and Burford Capital, as noted in Part III of this Note. Through the use

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231. BEISNER ET AL., *supra* note 29, at 7–8.

232. *Id.* at 7; see also Molot, *supra* note 20, at 111–13.

233. See BEISNER ET AL., *supra* note 29, at 7 (“[L]itigation-financing arrangements undercut the plaintiff’s control over his or her claim because investors inherently desire to protect their investment . . .”).

234. N.Y. COMP. CODES R. & REGS. tit. 22, § 603.7 (2012).

235. *In re World Trade Ctr. Disaster Site Litig.*, No. 21 MC 100(AKH), 2010 WL 3582921, at \*2 (S.D.N.Y. Sept. 14, 2010); see also Robert Gearty, *Law Firm Worby Groner Edelman & Napoli Bern That Represented Ground Zero Heroes Agrees to Trim Fees*, N.Y. DAILY NEWS (Sept. 2, 2010, 4:00 AM), <http://www.nydailynews.com/new-york/law-firm-worby-groner-edelman-napoli-bern-represented-ground-zero-heroes-agrees-trim-fees-article-1.439563>.

of subsidiaries and stage financing—where money is invested in blocks throughout the course of litigation as needed, rather than in one lump sum—Burford invested \$4 million with the possibility of a total \$15 million in the Ecuadorian’s claim.<sup>236</sup> The way Burford structured the contract ensured that they would receive any potential settlement or award before anyone else did.<sup>237</sup> Fortune magazine analyzed the contract shortly after it was made public in court proceedings:

If Burford ponies up the full \$15 million and the plaintiffs end up recovering \$1 billion, Burford will get \$55 million. If the plaintiffs recover \$2 billion, Burford gets \$111 million, and so on . . . . If the plaintiffs recover less than \$1 billion . . . Burford still gets the same payout it would have received if there had been a \$1 billion recovery. . . . In that event, by the way, the remaining [amount of the settlement minus Burford’s \$55 million] would not go to the plaintiffs; rather, it would go to other investors, who are also supposed to get their returns on investment (not just their capital outlays) before the plaintiffs start seeing a dime. In fact, under the “distribution waterfall” set up by the 75-page contract, it is only after eight tiers of funders, attorneys, and “advisers” (including the plaintiffs’ e-discovery contractor) have fed at the trough that “the balance (if any) shall be paid to the claimants.”<sup>238</sup>

The concern in each of the situations in this section is the same—the client’s interests are displaced by the financial interests of the attorney or the financier. Such an arrangement is incongruous with the basic notion that litigation should primarily benefit those privy to the substantive claim being litigated.

Simple rules can and should be adopted to prevent these outcomes. Consumer protection laws should be developed such that a lawyer cannot engage a financier without the knowledge and agreement of the plaintiff. Since the presence of a financier will undoubtedly affect how the case is litigated, the client needs to have knowledge of the relationship. Once the financier is engaged, an assortment of other rules are then triggered. Primarily, the financier should owe a fiduciary duty to the client, similar to the duty of loyalty that the attorney owes the client.<sup>239</sup> This fiduciary duty would accomplish several ends. First, this duty would require the financier to act in the best interest of the client, and to abide by the client’s wishes of when to end litigation; shareholders’ interest in maximizing returns to investment by continuing litigation through jury award will be supplanted by the client’s decision to settle earlier if she chooses.

Second, this fiduciary duty should limit the financier’s involvement in litigation to a role no greater than that played by the attorney. This rule would

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236. Steinitz, *supra* note 20, at 467.

237. *Id.* at 467–68.

238. Roger Parloff, *Have You Got a Piece of This Lawsuit?*, CNN MONEY (June 28, 2011, 2:06 PM), <http://fortune.com/2011/06/28/have-you-got-a-piece-of-this-lawsuit-2/>.

239. Steinitz, *supra* note 18, at 1328.

further the idea that the purpose of litigation is for the litigants to achieve the end that they desire. At no point can the financier direct the course of litigation; the client must at all times be able to end the litigation efforts when she chooses. The financier can act as a passive player in the litigation, only providing finance at agreed upon times. Or the financier can act as an advisor working in concert with the attorney on litigation efforts and strategy.

This fiduciary duty should also expose the financier to many of the same liabilities attorneys face. If an attorney files a claim that is wholly meritless or invalid, Federal Rule of Civil Procedure 11 permits the court to impose an “appropriate sanction” on the attorney and the attorney’s firm for violating the rule.<sup>240</sup> Similarly, a plaintiff that files a meritless or frivolous claim can be sued by the defendant through the common law claim of malicious prosecution of a civil action.<sup>241</sup> If a claim is financed by a third party, the third party should have an affirmative duty to investigate the legitimacy of the claim, otherwise the third party should be exposed to the same common law claim of malicious prosecution. Such a rule would act to prevent funds from financing meritless or frivolous litigation and encourage third parties to take an affirmative role in analyzing the merits of any investment in a case. Moreover, such an affirmative duty would encourage the third-party financier to become engaged in litigation strategy to ensure that the plaintiffs’ attorneys use the financing to further litigation efforts in legal and ethical ways.

Recently, the cost of not making such investigations or taking a continued involvement forced Burford Capital to relinquish any stake in the \$19 billion settlement reached against Chevron.<sup>242</sup> In court papers filed in April 2013, Burford claimed to have conducted “months of due diligence” on the case against Chevron before agreeing to finance the litigation efforts.<sup>243</sup> Despite the preinvestment analysis, Burford missed that Donziger and Patton Boggs, the plaintiffs’ attorneys, had made numerous false and misleading statements to courts in both the United States and Ecuador.<sup>244</sup> More than just false statements, by taking a passive role in the litigation, Burford missed that the plaintiffs’ attorneys might have bribed an Ecuadorian judge with \$500,000.<sup>245</sup> Burford also missed that a damage assessment supposedly drafted by a “neutral and independent” court-

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240. FED. R. CIV. P. 11(b).

241. DAN B. DOBBS & ELLEN M. BUBLICK, *ADVANCED TORTS: ECONOMIC AND DIGNITARY TORTS: BUSINESS, COMMERCIAL AND INTANGIBLE HARMS* 280–82 (2006).

242. Roger Parloff, *Litigation Finance Firm in Chevron Case Says It Was Duped By Patton Boggs*, FORTUNE (Apr. 17, 2013 5:16 PM), <http://features.blogs.fortune.cnn.com/2013/04/17/burford-patton-boggs-chevron-suit/>.

243. Declaration of Christopher Bogart at ¶ 4, *Chevron v. Donziger*, 1:11-cv-00691-LAK-JCF (S.D.N.Y. Feb. 1, 2011).

244. *Id.*

245. Parloff, *supra* note 242.

appointed expert was actually ghost written by the plaintiffs' lawyers.<sup>246</sup> As a result of the rampant fraud in the case, Burford sold its stake in the claim and relinquished any right the firm had to a portion of the award.<sup>247</sup> Had Burford been involved in the litigation efforts, it could have possibly ensured that such fraud never would have happened.

Secondly, the client should be notified of how the presence of a litigation financier will affect the client's portion of any settlement or award. In Burford's arrangement with the Ecuadorians, Burford set a recovery floor that established the lowest amount they would recover from any settlement or reward.<sup>248</sup> This floor, however, was far more than what they invested and represented what Burford likely saw as a fair return on their investment, irrespective of what the plaintiffs fairly deserved. But financiers should only receive priority in recovery up to the amount they invested (the amount they invested as representative to the amount of risk they assumed). Once they have recovered their initial investment, they only receive the percentage of the settlement or award they agreed to, rather than a guaranteed minimum return up to the percentage stake.<sup>249</sup> Such an arrangement would still serve the interest of financiers, in that they will recover their investment before the lawyer or client recovers anything. This structure also rewards the financier for the risk they assumed from the client and attorney by providing finance. But this structure also acknowledges that the client and attorney deserve a portion of the reward that represents the amount of risk they assumed.

Once the financier has recovered their initial investment, the client should have to pay for the financier's stake of the claim. As discussed earlier, several states have recognized that plaintiffs should have to pay for certain fees associated with litigation.<sup>250</sup> Passing some fees associated with litigation finance onto the plaintiff does not seem wholly unfair. In a noncontingency fee arrangement between an attorney and a client, the client pays the hourly fees of the attorney plus any fees that accumulate during the course of litigation, including expert witness fees, filing fees, discovery fees, and so on; the contingency fee only represents a sum equal to a reasonable number of hours billed out at a reasonable hourly rate.<sup>251</sup>

The portion of the settlement due to the financier should be treated similarly

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246. *Id.*

247. *Id.*

248. Steinitz, *supra* note 20, at 468.

249. As an example, imagine a stylized arrangement based on the \$18 billion award in the Chevron litigation in which Chevron was the only investor. If Burford invested \$4 million in exchange for a 1.5% stake in the recovery, Burford should recover its \$4 million investment initially plus \$270 million from its share of the recovery, for a total of \$274 million. But if recovery was only \$100 million, Burford should only recover its \$4 million investment plus \$1.5 million.

250. *See supra* note 234 and accompanying text.

251. *Lindy Bros. Builders, Inc. v. Am. Radiator & Standard Sanitary Corp.*, 487 F.2d 161, 166–69 (3d Cir. 1973), *vacated*, 540 F.2d 102 (3d Cir. 1976); Steinitz, *supra* note 18, at 1306 n.143.

to other fees accumulated during litigation (so long as the invested money is only used to further the client's litigation efforts, as opposed to paying for the fixed costs incurred by the attorney's firm or for litigating other matters). This is because the money invested is used to acquire the same types of services that the client would have to pay for if financing was not used: hiring more attorneys, hiring more expert witnesses, paying for deeper investigations, and so forth. The clients simply have to be told from the outset that their portion of the settlement or award will be reduced accordingly.<sup>252</sup>

#### D. *Protecting Confidentiality*

Next, critics claim that bringing on a financier will violate confidentiality. Critics claim that before financiers will agree to invest in a suit, they will want to know details of the claim, which might include information given to the attorney by the client orally or in writing, as well as other information gathered or prepared by the attorney in anticipation of the litigation.<sup>253</sup> Generally, these materials are considered confidential. Communications between client and the attorney are considered confidential through the attorney-client privilege and "documents and tangible things that are prepared in anticipation of litigation or for trial by or for another party or its representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent)" are also considered confidential under the work-product doctrine.<sup>254</sup> But these communications and materials lose the protection of confidentiality and can be compelled for disclosure during discovery if the plaintiff or attorney waives either privilege by disclosing the information to a third party, such as a litigation financier.<sup>255</sup>

These criticisms might be moot, however, because some financiers make investment decisions without the use of confidential information. Indeed, Kenneth Doroshow, a managing director at Burford told a bar association group in Massachusetts in early 2012 that "[w]e don't ask for privileged information . . . . We diligence around privilege."<sup>256</sup>

But even if the financier would want access to confidential information,

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252. Continuing the hypothetical arrangement between the Ecuadorian plaintiffs, Donziger, and Burford, if the plaintiffs agreed to a basic contingency fee contract with Donziger, then the plaintiffs would be required to pay the \$270 million fee to Burford from their portion of the settlement. How much they are entitled to relative to how much Donziger is entitled to would be up to the court. While contingency fee contracts typically stipulate that the attorney is entitled to one-third of any recovery, a court in this stylized hypothetical would not likely approve Donziger to receive \$6 billion because of lodestar standards with set attorney contingency fees based on reasonable hourly rates multiplied by a reasonable number of billable hours, the product of which is adjusted by several factors. See *Lindy Bros. Builders*, 487 F.2d at 166–69; Steinitz, *supra* note 18, at 1306.

253. BEISNER ET AL., *supra* note 29, at 8.

254. FED. R. CIV. P. 26(b)(3)(A); *Hickman v. Taylor*, 329 U.S. 495, 510 (1947).

255. *Westinghouse Elec. Corp. v. Republic of Philippines*, 951 F.2d 1414, 1424 (3d Cir. 1991).

256. McDonald, *supra* note 16.

courts have afforded broad protections to communications and work product. Beyond material prepared by the client's attorney, the work-product doctrine also applies to documents prepared in anticipation of litigation "by or for" any other "representative" of the party, as codified in Federal Rules of Civil Procedure Rule 26(b)(3).<sup>257</sup> Furthermore, in *Republic of Philippines v. Westinghouse Electric Corp.*, the Third Circuit ruled that disclosure of material considered as work product to a third party does not amount to a waiver unless it would "enable an adversary to gain access to the information."<sup>258</sup> Other courts have acknowledged the need to share confidential information with financiers, allowing the communications and documents exchanged to remain confidential. In *Mondis Technology, Ltd. v. LG Electronics, Inc.*, the court held that documents shared with potential financiers were considered work product and not available for discovery because sharing documents considered work product with potential financiers "did not substantially increase the likelihood that an adversary would come into possession of the materials."<sup>259</sup>

Another strategy to keep the documents confidential would be for the attorney and financier to codify their common interest in the outcome of the litigation by signing a nondisclosure agreement. The nondisclosure agreement would stipulate that the contracting parties have a common interest in the outcome of the litigation. This agreement would then trigger the common interest doctrine. The common interest doctrine protects from discovery documents exchanged between "attorneys representing different clients with similar legal interests."<sup>260</sup> In the case of litigation finance, the attorneys involved technically represent different clients. The attorneys who work for the financier represent the financier, and the attorney who works for the client represents the client; all of those attorneys share a similar legal interest in the outcome of the case being financed. By signing a nondisclosure agreement that stipulates confidentiality in all documents exchanged and outlines the common interest shared in the outcome of the litigation, courts will be more inclined to give protection to documents exchanged. Indeed, in litigation between Google and Walker Digital, where Walker Digital (the plaintiff) received litigation funding from IP Navigation Group, United States District Court Judge Sue L. Robinson of Delaware ruled

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257. See FED. R. CIV. P. 26(b)(3)(A) (defining "representative" as "including" an "attorney, consultant, surety, indemnitor, insurer, or agent"); *United States v. Adlman*, 134 F.3d 1194, 1195 (2d Cir. 1998); see also FED. R. CIV. P. 26 advisory committee's note (1970 Amendment) (subdivision (b)(3) applies "to materials prepared in anticipation of litigation or preparation for trial by or for a party or any representative acting on his behalf" (emphasis added)); Memorandum in Support of the Joint Motion for Protective Order and to Quash the Third-party Subpoenas to Burford Group LLC, Gelnavy Capital LLC, and Litigating Risk Solutions LLC at 8–9, *Devon IT, Inc. v. IBM Corp.*, 2:10-cv-02899-JHS (E.D. Pa. Jan. 27, 2012).

258. *Westinghouse*, 951 F.2d at 1428.

259. *Mondis Tech., Ltd. v. LG Elecs., Inc.*, No. 2:07-CV-565-TJW-CE, 2011 WL 1714304, at \*3 (E.D. Tex. May 4, 2011).

260. *In re Teleglobe Commc'ns Corp.*, 493 F.3d 345, 364 (3d Cir. 2007).

that “Walker Digital and IPNav do share a common interest and, therefore, any Walker Digital communications protected by the attorney-client privilege or work product doctrine do not lose that protection simply because they have been disclosed to IPNav.”<sup>261</sup>

While the newest form of TPLF raises certain ethical, legal, and moral concerns, the practice should not be banned. Several states have already removed antiquated laws from their civil codes that would prevent the expansion of TPLF, while others have made efforts to expressly permit the practice. Other professional rules can be easily amended to better allow for TPLF.

#### CONCLUSION

Imagine a situation in which an injured person walks into a contingency fee lawyer’s office. The potential client tells the lawyer that her supervisor at work sexually harassed her; the harassment occurred over many months, several of her coworkers observed the episodes, and she reported each episode to the company’s human resources department. The potential client told the lawyer that when she finally resisted the harassment, the supervisor fired her.

As the client tells the attorney the facts, he thinks how much will it cost me to plead this and survive a Rule 12(b)(6)?

Pre-*Twombly*, the lawyer would have needed to plead the simplest facts that the potential client gave to him: that she was an employee at the certain business, the name of her supervisor, and the basic details of the harassment. Any other facts that would be necessary to convince the jury of the harassment or to compel the company to settle would be uncovered during discovery: the client’s employment records, records of the client’s reports of the harassment, records of efforts made by the company to remedy the harassment, and so forth.

But now, with a heightened pleading standard, the lawyer must investigate those claims before he files so he can include the facts in the complaint. He might need to interview the client further to determine which coworkers observed the harassment, then he will need to interview the coworkers to get more facts regarding the client’s story. He might need to interview any doctors or therapists the client saw after the harassment began. He might also need to research whether the company has had past incidents of sexual harassment.

All of this research takes time—time that the lawyer would have otherwise been spending on other cases, which would generate cash flow; or the time of an investigator for which the attorney pays. If the attorney lacks the cash, he might decline the case. The potential client might never see justice.

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261. Walker Digital, LLC v. Google, Inc., No. 11-309-SLR, 2013 WL 9600775, at \*1 (D. Del. Feb. 12, 2013); see also Devon IT v. IBM Corp., 2:10-cv-02899-JHS, 2012 WL 4748160, at \*1 n.1 (E.D. Pa. Sept. 27, 2012).



But now imagine a situation in which the lawyer can call a financier who will provide the cash necessary to conduct the prefiling investigation.

The potential benefits to society from expanding the practice are great. Since *Marbury v. Madison*, courts have acknowledged the right of potential litigants to have their claims heard by a judge. While the rulings in *Iqbal* and *Twombly* have presented potential litigants with a hurdle, the newest form of litigation finance could help them make the jump.

While critics express several valid concerns about the expansion of litigation finance, this new wave of litigation finance simply continues a long practiced tradition of third-parties' involvement in lawsuits. Rather than heeding to the fears of critics, bar associations and politicians should be mindful of the costs of the practice remaining unregulated, as seen in the Chevron litigation. But a full ban on the practice at this stage—in its infancy—seems imprudent, as we have yet to see how litigation finance might benefit more people as it becomes more democratized. Any full proscription on the practice could bar litigants with valid claims from accessing justice.

