THE COMPLETE LITIGATION FINANCE GUIDE

FOR PLAINTIFF'S ATTORNEYS

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This guide will provide you with information about third-party litigation finance as a plaintiff's attorney, including leveraging finance options to improve your case outcomes and increase access to justice for your clients.

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I. INTRODUCTION

THE SIZE OF YOUR WALLET SHOULDN'T DETERMINE THE OUTCOME OF YOUR CASE.

As an attorney, you invest in your case to ensure the best outcome for your clients. If your cases get stuck or don't resolve promptly, your resources are frozen. The problem worsens because many plaintiff's attorneys offer their services on a contingency basis.

The result? It could be months or years before you see a return on your investment, leaving you unable to take on new cases to grow your portfolio and business.

You work to represent plaintiffs in mass tort, personal injury, and employment lawsuits, but defendants can have what feels like an endless coffer of resources to shut down your client's case.

Plaintiff's attorneys do mental gymnastics every day. Pretrial discovery activities, like depositions, are weighed against the case-value benefit. Third-party litigation financing can help attorneys refocus on representing their clients without cost restraints.

In recent years third-party litigation finance has become more common. Typically, litigation funders agree to share a claimant's risk and provide financial assistance in exchange for a share of the potential recovery.

On the plaintiff's side, funding is usually provided as a non-recourse investment, which means no payment is required unless the case resolves favorably. Additionally, the investor must be a passive participant and maintain no control over the litigation process or the attorney-client relationship.

While this funding practice is gaining momentum, plaintiff's attorneys should have a strong understanding of litigation finance.

This guide gives plaintiff's attorneys a comprehensive understanding of the third-party litigation finance process. It also includes information on regulations, benefits, types of funding, common criticisms and a look at the industry's future.

Discover how litigation financing helps level the judicial playing field and gives you a competitive advantage as a plaintiff's attorney or firm owner.

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II. LITIGATION FINANCE FOR PLAINTIFF'S ATTORNEYS

WHAT IS LITIGATION FINANCE?

Litigation finance is the practice of a third party providing funding for a claimant or their counsel in the litigation process, typically in exchange for a portion of the case recovery. Depending on the arrangement with the lender and federal and local regulations, it is typically a non-recourse investment.

In 2018, the American Bar Association Journal reported that a third of lawyers surveyed used litigation finance to help fund cases, and 70% of firms said they were likely to use it in the next two years.

Litigation funding can pay for living expenses, legal expenses, attorney's fees, court reporting, litigation support services, expert witness fees, and generalized court expenses.

Litigants seeking to pursue a claim often lack access to the same resources as the defense firms or insurance companies they're up against. Litigation finance empowers plaintiff's attorneys by providing them with the capital to access justice for their clients.

ORIGINS OF LITIGATION FINANCE

The practice of litigation finance in the United States is relatively new and has only been around for about 30 years. In Australia in the mid-1990s, litigation finance began to gain traction following the legalization of class-action lawsuits. Before that, in the United Kingdom, the Criminal Law Act of 1967 decriminalized maintenance and champerty.

Scholars of the industry assert that litigation funding first originated in the historical European legal principles of champerty and maintenance and arrived in the United States through British common law. This legislation aimed to prevent speculation in litigation.

The modern practice in the United States drew significant influence from funding practices overseas. In the late 1990s, industry pioneers began grassroots funding of worthy plaintiffs' claims to provide them with access to the courts. The first funding arrangements were not well documented, and skeptics questioned the ethical implications of external investment in pending litigation.

At the state level, litigation finance in commercial litigation and arbitration is gaining popularity. However, there are still limits on commercial funding arrangements in states where champerty and maintenance were once utilized legislation.

ETHICS OPINIONS AND REGULATIONS

Litigation finance is primarily regulated at the state level and is subject to legislation, ethics opinions, case precedents, and agreements with local regulatory organizations. Few states agree on how to handle litigation finance. Permissibility of recourse versus non-recourse funding arrangements also varies state by state.

As US legislation has evolved, litigation finance has become more common due to the clear benefit to plaintiff's lawyers, who are often out-resourced by defendants. Today, the litigation finance industry is essential in commercial and consumer lawsuits and is likely to continue expanding.

1. Champerty, Maintenance, and Barratry

Champerty, maintenance and barratry are common law doctrines that have historically prohibited third-party litigation finance. Maintenance is the act of a third party promoting or maintaining a lawsuit. Champerty is commonly referred to as maintenance for profit, for a portion of the recovery of a lawsuit. Barratry is the act of encouraging lawsuits between others to create legal business for one's gain and profit. This legislation has been abolished in many states and is in the process of being repealed in others.

2. Attorney-Client Privilege and Attorney Work-Product Immunity

Attorney-client privilege refers to a legal right that works to keep confidential communications between an attorney and their client secret. The privilege is asserted if there is a legal demand for attorney-client communications like a discovery request.

Privilege only exists when there is an attorney-client relationship. The attorney-client privilege does not protect communications with an investor because the investor is not acting as the plaintiff's counsel.

Attorney work-product privilege permits attorneys to withhold documents from production and other tangible things prepared in anticipation of litigation by or for another party.

Several relevant case precedents support the view that litigation finance transactions do not impact these standards. The key takeaways from those precedents are:

- Investors should not require access to privileged attorney-client communications, but the person seeking the funding is free to tell a prospective funder anything other than what the client has communicated to the attorney
- An investor can receive substantial information from the plaintiff's attorney about the claim

- The presence of a litigation funder does not waive work-product protection because it does not increase the likelihood that an adversary would obtain the materials.
- Work-product covers investors because they share a common interest in the outcome of a case and have signed a non-disclosure agreement

3. Ethics Opinions

Formal ethics opinions on litigation finance vary significantly across state lines. However, in addition to champerty, maintenance, barratry, attorney-client privilege and attorney work-product immunity, many focus on the concepts of control and disclosure.

A. CONTROL

Several ethics rules require that the claimant and attorney control the litigation strategy, and the third-party funder is not permitted to shape the approach. For example, the American Bar Association's Model Rules of Professional Conduct 1.2(a) states, *"[a] lawyer shall abide by a client's decisions concerning the objectives of representation" and "a client's decision whether to settle a matter."*

Rule 1.8(f) permits an investor to pay a lawyer's fee only if *"there is no interference with the lawyer's independence of professional judgment or with the client-lawyer relationship."* Rule 2.1 requires the attorney to *"exercise independent professional judgment"* on behalf of a client.

B. DISCLOSURE

Disclosure is more focused on process than the legality of litigation finance. The principle is relevant during discovery and regarding the mandatory disclosure of funding agreements to the courts.

Opposing counsel can request documents related to any plaintiff's litigation finance agreements. According to the Federal Rules of Civil Procedure 26(b)(1), discovery rules allow courts to require disclosure of *"any nonprivileged matter that is relevant to any party's claim or defense and proportional to the needs of the case."* Most relevant case precedents hold that funding documents do not need to be disclosed because they are irrelevant to the facts of a case.

Adversaries of litigation finance would like to require mandatory disclosure of the total amount of all funding agreements. Advocates for litigation finance oppose mandatory disclosure because of its impact on the judge or jury's opinion of the plaintiff. Disclosure typically only benefits the defendant. Generally, mandatory disclosure is not required at the state or court level.

Finally, suppose an attorney borrows funds from an investor to represent a client. In that case, most ethics opinions agree that attorneys must disclose any litigation finance they have received in the attorney-client agreement.

III. TYPES OF LITIGATION FINANCING

Investors generally specialize in either consumer or commercial litigation financing and provide capital typically in exchange for a portion of the recovery. As the industry evolves, investing organizations are also exploring innovative ways to fund the litigation process for individuals, firms and corporations.

COMMERCIAL LITIGATION FINANCING

Commercial financing is typically a non-recourse investment in commercial disputes where the claimant is a company or an individual. Generally, the claimant agrees to pay a portion of the recovery to the funding organization.

Commercial litigation funders typically provide capital for high-value, complex cases, including: **antitrust, breach of contract or fiduciary duty, intellectual property,** and **insurance.**

Parties are typically business entities with sophisticated counsel. On average, commercial litigation financing is in the $1 million range. There are many types of commercial financing, but single-case and portfolio financing are most common in the United States.

SINGLE-CASE FINANCING

This type provides capital for legal finance and expenses to support a single case, with a non-recourse return structure.

Single-case financing can cover fees incurred by the claimant's lawyers and cover costs related to e-disclosure, expert witnesses, and court fees.

PORTFOLIO FINANCING

A legal finance portfolio usually consists of four or more cases litigated by a law firm or company on a full or partial contingency basis. There is no limit to how many cases comprise a portfolio.

For firms, investment recovery occurs when one or more of the cases in the portfolio closes. For corporations, the investment is repaid from future recoveries or according to the terms of the original agreement.

Portfolio funding agreements can be used to fund cases for a plaintiff, defense, or a mix of both. The portfolio is constructed by evaluating the risk and return on a group of cases.

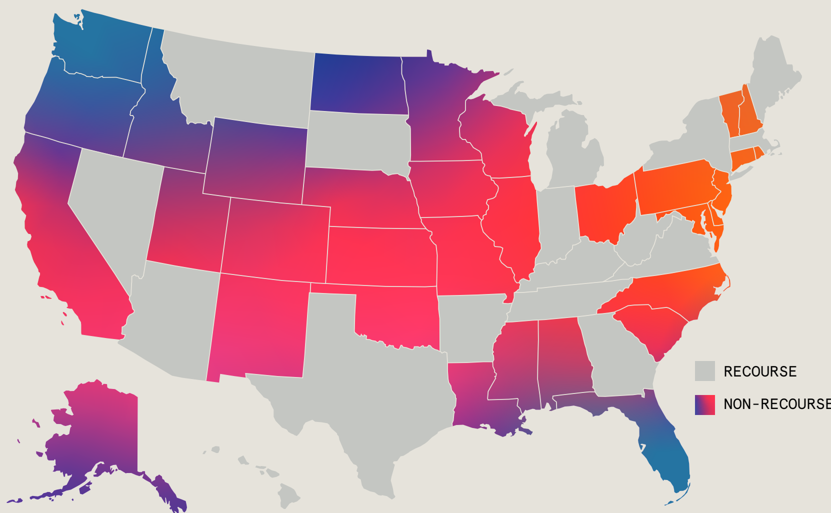
Prominent commercial financing companies include LexShares, Burford Capital, and Pravati Capital.

INNOVATIVE LITIGATION FINANCING

The traditional financing options discussed don't address the needs of firms representing plaintiffs in personal injury, employment, and other cases with lower expected outcomes. Plaintiff's firms looking for a micro-investment are left with few favorable financing options.

Court reporting, and litigation support services, represent a considerable portion of a firm's investment in any case. To address this need, Steno is pioneering a new type of litigation financing called DelayPay. Steno provides plaintiff's attorneys with deferred payment court reporting and litigation support services.

In states where regulations permit it, services are non-recourse; no payment is due if the case doesn't resolve in favor of the plaintiff. This map denotes states that have regulations permitting or prohibiting non-recourse financing for court reporting and litigation support services.



STATES PERMITTING NON-RECOURSE SERVICES

Steno's payment process combines micro-financing and commercial litigation financing to create a solution to improve plaintiff's access to justice and level the playing field for attorneys battling huge defense firm coffers.

Steno partners with a debt facility to borrow against the total value of the services provided. This process enables Steno to provide capital to pay court reporters and fund business operations while clients' cases progress toward resolution.

In an average commercial litigation arrangement, a funder may invest $1 million in a single case or portfolio. Steno's average investment is less than $10,000 per case.

Other litigation support services providers don't typically provide this type of payment structure, or if they do, they require an application process, pre-approval, or repayment with interest. Steno's DelayPay doesn't require application, approval, waiting period, or interest repayment.

IV. THE BENEFITS OF LITIGATION FINANCE

Litigation finance can benefit plaintiffs, attorneys, firms, and investors. It can improve access to the justice system, aid in financial planning and forecasting, open the door for business development, and provide portfolio diversification opportunities.

PLAINTIFFS

Plaintiffs are typically up against major corporations or insurance companies with endless financial resources to fight their claims. If a case drags on for years, that could have catastrophic impacts on the claimant's financial situation. Additionally, if an individual cannot work or afford living expenses, funding can be used to cover personal living expenses. Lastly, the individual or company may access higher-quality legal resources than they could without an external investor and pursue their claim to the fullest extent.

PLAINTIFF'S ATTORNEYS AND LAW FIRMS

Plaintiff's attorneys often represent individuals who can lack the resources to pursue their claim in the judicial system. Litigation finance can cover attorney fees, e-disclosure, expert witnesses, court fees, and other costs incurred in the litigation process. External funding can also reduce the risk of running out of capital in the middle of the process.

Firms can permit their attorneys to enter into flexible repayment agreements, enabling them to take on more clients. Freeing up the firm's capital makes it possible for the firm to build its portfolio and invest in improving elements of its operational processes, including:

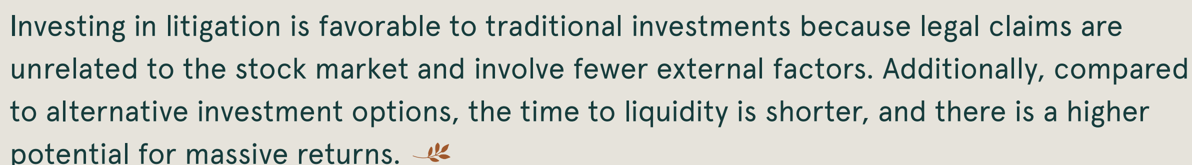
- Hiring legal support staff
- Automating the client intake process
- Establishing marketing strategies
- Trial presentation material development
- Expanding their practice

Finally, litigation financing helps attorneys achieve recoveries for their clients that reflect the merits and damages of the case.

INVESTORS

Bloomberg Law estimates investors in the litigation finance industry have increased their assets by 32% since 2019. Funders find litigation an attractive investment because the industry has steadily grown over the last 20 years.

Investing in litigation is favorable to traditional investments because legal claims are unrelated to the stock market and involve fewer external factors. Additionally, compared to alternative investment options, the time to liquidity is shorter, and there is a higher potential for massive returns.



V. UNDERSTANDING THE INVESTMENT PROCESS

In traditional litigation financing, there are several steps from the initial application to the dispersal of funds and repayment. Every investment company has unique procedures for evaluating cases, but most follow the steps discussed below.

DETERMINING IF A CASE WOULD BENEFIT FROM INVESTMENT

The average personal injury or employment case lasts approximately two years. Mass torts and malpractice claims can span even longer.

More prolonged cases can have catastrophic impacts on a plaintiff, affecting their daily life and ability to cover their expenses. Plaintiff's attorneys often invest capital in cases and don't expect repayment until the case resolves. Without litigation finance, the likelihood of fully representing a claim with limited capital is low.

Third-party financing empowers plaintiff's attorneys to continue living and working while pursuing justice under the law.

When considering if third-party litigation finance could benefit a case, attorneys should answer these questions:

"Do I have the budget and means to represent the claimant in this case?"

"Are my firm's resources well matched against the opposing counsel's firm, or am I financially outmatched?"

"Do litigation finance companies typically invest in this type of claim?"

"How strong is the claim on the merits?"

SUBMITTING A CASE FOR CONSIDERATION

Select a reputable funding institution with a credible track record of investing in similar types of claims. It's preferable to work with a funder who has the capital already and does not need to seek external investment. Each litigation finance company will have unique criteria for selecting its investments and receives more applications than they can accept.

Provide as much information as possible, including case type, jurisdiction location, stage of the litigation process, current budget, details about the legal teams on both sides, case documents and materials, and anything else that might benefit the investor to review.

Attorneys should follow these best practices when presenting a case for funding:

- Make an excellent first impression
- Don’t hide negative facts of the case; in the diligence process, underwriters will find them
- Be prepared to share case materials, from deposition transcripts to written settlement offers
- Understand which case types the company typically funds

SIGNING A NON DISCLOSURE AGREEMENT

Litigation finance companies will require a non-disclosure agreement (NDA) before proceeding with the diligence process and reviewing a case in detail. This step is essential because it ensures all parties maintain confidentiality and adhere to the attorney work-product legislation.

Opposing counsel can request disclosure of all communications with a litigation finance company in discovery. However, case presidents to date have found that these communications are not discoverable, and an NDA helps strengthen this protection.

THE DILIGENCE PROCESS AND CASE SELECTION CRITERIA

Once the funder decides to evaluate an application, they may require the attorney to enter into an exclusivity agreement to provide them the necessary time to assess the merits of a case.

Once this initial, non-binding agreement has been reached, the funder enters into their diligence process and evaluates the case against a variety of factors, including:

- Potential recovery amounts compared to the claim’s complexity
- The estimated budget compared to additional investment requests
- The likelihood of winning in court
- The other parties involved, who hold a stake in the case
- The state or federal jurisdiction where the claim was filed
- Potential counterclaims from the defense

The funder evaluates these factors to determine the likelihood that their investment will provide a return. They typically engage various subject matter experts, and the process can last one or two months, depending on the complexity of the claim.

THE LITIGATION FINANCE INVESTMENT AGREEMENT

Once an application makes it through the diligence process, negotiating the funding agreement begins.

Many litigation finance companies have limited transparency, so providing a reliable industry standard for investment agreement structures is challenging. Additionally, each case includes different factors that could impact the agreement.

The American Bar Association adopted best practices for third-party litigation funding in 2020. The below passage is an excerpt from the resolution on documentation and structure of funding agreements:

> *"The funding agreement should be drafted to assure that: (a) the client retains control of the litigation (including, for example, decisions as to whether to settle or discontinue the litigation as opposed to proceeding to trial or verdict) and (b) that the lawyer retains independent professional judgment. Lawyers advising clients on litigation funding should be careful about arrangements that appear to give a majority interest in a lawsuit to the funder because this may give rise to an argument that the funder has assumed control of the lawsuit, a role that belongs to the client. While there may be cases in which more than a majority of the recovery goes to the funder for a variety of reasons, control of key litigation decisions, including with respect to settlement, should remain with the client in all circumstances. The non-recourse nature of the agreement should be clearly set forth. Recourse can take many forms, including liability for a variety of wrongs caused [by] the funder. Merger and integration clauses, as well as robust waiver provisions, are a must."*

In summary, attorneys should ensure that:

01

The funder does not obtain any control over the litigation strategy

02

They retain independent professional judgment

03

It is clear if the agreement is structured as recourse or non-recourse

04

Pricing should be fair, & the litigation financier should not receive a majority of the recovery

MAINTENANCE AND MONITORING

Once a consensus is reached and the investment agreement is signed, the case is considered funded. Capital may be dispersed in a lump sum or installments depending on the payment structuring agreement.

Litigation finance companies must ensure their investment is well maintained throughout the litigation process. The attorney should treat the company as a partner, be communicative and provide updates on developments in the case.

While the funder should not guide the case strategy, they can help if a case takes an unexpected turn. Funders often employ attorneys as part of their account management team and may be able to provide resources to put the case back on track.

VI. CRITICISMS OF LITIGATION FINANCE

Today, there are many skeptics of the litigation finance industry. Advocates view the practice as an equalizing force, improving access to justice for claimants who lack the wealth required to advocate for themselves independently.

Opponents view litigation finance as a threat to the integrity of the legal system and an ethical gray area. Opposition to innovation in most industries stems from a lack of understanding. Below are common criticisms of the litigation finance sector and explanations that dispel those misconceptions:

Does litigation finance incentivize the frivolous pursuit of a lawsuit?

No, litigation finance companies only consider investing in a case once it has been established and the litigation process has started. They will not evaluate a claim until it is filed with the courts. Additionally, funding institutions are highly selective with their investments and are unlikely to advance capital to fund a case they do not believe will resolve in their favor. Most funding agreements are structured as non-recourse, meaning that the funder will not receive a payment if the case is unsuccessful. For attorneys, litigation finance does not incentivize the pursuit of a case because the funding can only be used for legal expenses, not for operational or administrative costs.

Isn't litigation finance just a loan?

No. Litigation financing is typically non-recourse, while loans are always recourse. Litigation financiers only recover their investment if the claim resolves in their favor. Loans require repayment of both the principal and interest, regardless of the outcome of a case.

Does litigation finance cause a conflict of interest?

No. State and local regulations expressly prohibit the third-party funder from controlling the litigation strategy.

Attorneys are also required to maintain independent professional judgment and protect the interest of their client above the interest of the investor.

Does litigation finance deprive plaintiffs of reasonable damages?

No. This question stems from the belief that funding agreements favor the investor over the client. However, once the case resolves, repaying the investor and the attorney is necessary.

The investor takes a substantial risk investing in a case with no clear timeline for repayment or guaranteed return. The attorney provides their expertise and service on a contingency basis and is not paid until the case resolves.

In the creation of the investment agreement, the plaintiff's attorney should negotiate fair repayment terms, ensuring that the funder does not receive the majority of the recovery.

VII. THE FUTURE OF LITIGATION FINANCE FOR PLAINTIFF'S ATTORNEYS

The litigation finance industry, while gaining traction, is still in its nascent stage. In 2022 and beyond, expect the industry to grow, particularly as the economy starts to slow down and plaintiff firms explore nontraditional ways to finance their cases.

New players are also starting to enter the litigation finance space, historically controlled by a few large multinational companies. These new entrants are looking for ways to make litigation financing available to firms and litigants that previously did not have access to this type of capital.

There are three key areas where Steno predicts the industry will evolve in the future:

01 Finance, technology and services providers will continue to consolidate their offerings.

02 As financial markets change globally, capital investments will continue to migrate toward safer sectors.

03 Local regulations and policies will shift and make room for innovations that were not previously possible, and there will be more advocacy for transparency in litigation finance.

Consolidation of services is an essential element of Steno's ethos as a company. Steno provides excellent court reporting for depositions, combined with innovative technology and microfinancing to create a single solution to a problem that attorneys relied on various vendors to solve.

Steno is pioneering this shift toward consolidation but believes that other companies will begin to evolve in the same way. Law firms rely on various vendors for support in the litigation process. If others can follow in Steno's footsteps, that will create massive improvements in the litigation process for plaintiff's attorneys.

Secondarily, more capital will enter the litigation finance market as macro factors change. This has already started to happen, and the industry has been experiencing exponential growth in the last few years.

Historically, when the broader economy downturns, funds migrate to safer sectors. The legal industry is inherently safer than traditional investments because of the low risk and high potential for an outsized return on investment.

Finally, more local regulatory bodies will fight for standardized rules on litigation financing. Consumer advocacy groups are rallying around plaintiffs to increase their access to justice by removing financial constraints. They advocate for maintaining the non-disclosure asset status so that utilizing this essential resource doesn't hurt a plaintiff's credibility or claim in a court of law.

The future of litigation finance for plaintiff's attorneys in the US is exciting. Advancements in the industry will continue to increase access to justice for the majority of Americans, historically reserved for the wealthy minority.

VIII. ABOUT STENO

Steno is a leading court reporting and litigation support services agency pioneering a new style of litigation financing. Instead of capital, Steno provides services with no upfront cost until the case closes and with no interest or price fluctuations based on the recovery size. Founded in 2018 and headquartered in Los Angeles, Steno serves attorneys across the United States. Visit steno.com for more information.

Greg Hong is the author of this guide and Co-Founder and Chief Executive Officer at Steno. He leads the executive team, serves as liaison to the board of directors and sets the course of the company's strategy. Greg was the Co-Founder and Chief Executive Officer of Reserve, a restaurant technology company. He strategically led the company to secure $45 million from investors before being acquired by Resy, American Express, in 2019. He has more than 18 years of experience building new companies.

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