AMERICAN BAR ASSOCIATION
COMMISSION ON ETHICS 20/20
INFORMATIONAL REPORT TO THE HOUSE OF DELEGATES

I. Introduction

Alternative litigation finance ("ALF") refers to the funding of litigation activities by entities other than the parties themselves, their counsel, or other entities with a preexisting contractual relationship with one of the parties, such as an indemnitor or a liability insurer. These transactions are generally between a party to litigation and a funding entity and involve an assignment of an interest in the proceeds from a cause of action. These activities have become increasingly prominent in recent years, leading to significant attention in the legal[1] and popular[2] press, scrutiny by state bar ethics committees,[3] and scholarly commentary.[4] The continuing

[1] *See, e.g.*, Terry Carter, *Cash Up Front: New Funding Sources Ease Strains on Plaintiffs' Lawyers*, 90 A.B.A. J. 34 (Oct. 2004); Lazar Emanuel, *An Overall View of the Litigation Funding Industry*, N.Y. PROF. RESP. REP., Feb. 2011; Leigh Jones, *Litigation Funding Begins to Take Off*, NAT'L L.J., Nov. 30, 2009; Eileen Libby, *Whose Lawsuit Is It?: Ethics Opinions Express Mixed Attitudes About Litigation Funding Arrangements*, 89 A.B.A. J. 36 (May 2003); Andrew Longstreth, *With Help From Litigation Funding Company, Simpson Thacher Wins $110 Million Verdict for Real Estate Firm in Phoenix Development Dispute*, AM. LAW. (July 27, 2010); Holly E. Louiseau, et al., *Third Party Financing of Commercial Litigation*, 24 IN-HOUSE LITIGATOR no. 4 (Summer 2010) & 25 IN-HOUSE LITIGATOR no. 1 (Fall 2010); Nate Raymond, *More Attorneys Exploring Third-Party Litigation Funding*, N.Y. L.J., June 4, 2010; Louis M. Solomon, *Third-Party Litigation Financing: It's Time to Let Clients Choose*, N.Y. L.J., Sept. 13, 2010.

[2] *See, e.g.*, Binyamin Appelbaum, *Investors Put Money on Lawsuits to Get Payouts*, N.Y. TIMES, Nov. 14, 2010; Binyamin Appelbaum, *Lawsuit Loans Add New Risk for the Injured*, N.Y. TIMES, Jan. 17, 2011; Binyamin Appelbaum, *Lawsuit Lenders Try to Limit Exposure to Consumer Rules*, N.Y. TIMES, Mar. 9, 2011; Jonathan D. Glater, *Investing in Lawsuits, for a Share of the Awards*, N.Y. TIMES, June 3, 2009); Vanessa O'Connell, *Funds Spring Up To Invest In High-Stakes Litigation*, WALL ST. J. (October 3, 2011); Roger Parloff, *Have You Got a Piece of This Lawsuit?*, FORTUNE, June 13, 2011, *available at* http://features.blogs.fortune.cnn.com/2011/06/28/have-you-got-a-piece-of-this-lawsuit-2/; *see also* Richard A. Epstein et al., Room for Debate, *Investing in Someone Else's Lawsuit*, N.Y. TIMES ONLINE, Nov. 15, 2010, *available at* http://www.nytimes.com/roomfordebate/2010/11/15/investing-in-someone-elses-lawsuit.

[3] *See, e.g.*, Ky. Bar Ass'n Ethics Comm., Formal Op. E-432 (2011); N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 2011-2 (2011); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 769 (2003).

[4] *See, e.g.*, Courtney R. Barksdale, *All That Glitters Isn't Gold: Analyzing the Costs and Benefits of Litigation Finance*, 26 REV. LITIG. 707 (2007); Paul Bond, Comment, *Making Champerty Work: An Invitation to State Action*, 150 U. PA. L. REV. 1297 (2002); Andrew Hananel & David Staubitz, *The Ethics of Law Loans in the Post*-Rancman *Era*, 17 GEO. J. LEGAL ETHICS 795 (2004); Jason Lyon, *Revolution in Progress: Third-Party Funding of American Litigation*, 58 UCLA L. REV. 571 (2010); Susan Lorde Martin, *Litigation Financing: Another Subprime Industry That Has a Place in the United States Market*, 53 VILL. L. REV. 83 (2008); Susan Lorde Martin, *The Litigation Financing Industry: The Wild West of Finance Should Be Tamed Not Outlawed*, 10 FORDHAM J. CORP. & FIN. L. 55 (2004); Susan Lorde Martin, *Financing Litigation On-Line: Usury and Other Obstacles*, 1 DEPAUL BUS. & COM. L.J. 85 (2002); Julia H. McLaughlin, *Litigation Funding: Charting a Legal and Ethical Course*, 31 VT. L. REV. 615 (2007); James E. Moliterno, *Broad Prohibition, Thin Rationale: The "Acquisition of an Interest and Financial Assistance in Litigation" Rules*, 16 GEO. J. LEGAL ETHICS 613 (2003); Jon T. Molot, *A Market in Litigation Risk*, 76 U. CHI. L. REV. 367 (2009); Douglas R. Richmond, *Other People's Money: The Ethics of Litigation Funding*, 56 MERCER L. REV. 649 (2005); 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 (2006); Anthony J. Sebok, *The Inauthentic Claim*, 64 VAND. L. REV. 61 (2011); Maya Steinitz, *Whose Claim is This Anyway, Third Party Litigation Funding*, 95 MINN. L. REV. 1268 (2011). Northwestern Law School hosted a public policy roundtable on Third Party Financing of Litigation in September 2009. For a list of participants and paper topics, and links to papers

globalization of the market for legal services makes alternative litigation finance available to clients in markets such as the United Kingdom, Australia, Germany and Spain, where it is legally permitted and generally available.

At least some forms of alternative litigation finance are permitted in many U.S. jurisdictions as well, but many lawyers are unfamiliar with the ethical issues presented by these transactions. The American Bar Association Commission on Ethics 20/20 therefore formed a Working Group on Alternative Litigation Finance to study the impact of these emerging transactional structures on the client-lawyer relationship and the professional responsibilities of lawyers.[5] The Working Group was directed to limit its consideration to the duties of lawyers representing clients who are considering or have obtained funding from alternative litigation finance suppliers. It did not consider social policy or normative issues, such as the desirability of this form of financing, or empirical controversies, such as the systemic effects of litigation financing on settlements (except insofar as this has an impact on the ethical obligations of lawyers), or the effect that alternative litigation finance may have on the incidence of litigation generally, or unmeritorious ("frivolous") lawsuits specifically.[6] Nor did the Working Group consider legislative or regulatory responses to perceived problems associated with alternative litigation finance in the consumer sector, such as excessive finance charges or inadequate disclosure. However, to the extent a lawyer is representing a client and advising or negotiating

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presented at the conference, see http://www.law.northwestern.edu/searlecenter/conference/roundtable/Searle_Third_Party_Financing_Agenda.pdf.

[5] The members of the Working Group are Philip H. Schaeffer (Co-Chair and Liaison to the Commission from the Standing Committee on Ethics and Professional Responsibility) Jeffrey B.Golden (Co-Chair and Commissioner), the Hon, Kathryn A. Oberly (Commissioner), Herman J. Russomanno (Commissioner), Professor Stephen Gillers (Commissioner), John C. Martin (ABA Section of Litigation), Charles D. Schmerler (ABA Section of International Law), Olav A. Haazen (Boise, Schiller & Flexner, LLP). Professors W. Bradley Wendel and Anthony Sebok serve as Reporter. Ellyn S. Rosen, Commission Counsel, and Ruth A. Woodruff provided counsel to the Working Group.

[6] The Working Group received comments from groups expressing various opinions about the effect of alternative litigation finance on the civil justice system. Critics of ALF predict that it will drive up the filing of lawsuits, without regard to their legal and factual merit, because suppliers will consider only the expected value of the investment, not the substantive merits of the claim. *See, e.g.*, Comments of the Am. Tort Reform Ass'n to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. (Feb. 15, 2011) (on file with author); Comments of the Prod. Liab. Advisory Council to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. (Feb. 15, 2011) (on file with author); Comments of the U.S. Chamber Inst. for Legal Reform to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. (Feb. 15, 2011) (on file with author). Proponents suggest there is some evidence that although the availability of alternative litigation finance is correlated with an increase in claim filing, its suppliers tend to fund strong claims, not frivolous ones. *See, e.g.* Martin, *supra* note 4; Moliterno, *supra* note 4; Molot, *supra* note 4; Rodak, *supra* note 4. Scholars also offer various views. For an empirical study, see Daniel L. Chen & David S. Abrams, *A Market for Justice: The Effect of Third Party Litigation Funding on Legal Outcomes,* Duke Law Sch., Working Paper, 2011), *available at* http://www.duke.edu/~dlc28/papers/MktJustice.pdf. Other scholars assert that alternative litigation finance better aligns the incentives of attorneys and clients, and also provides a strong signal of claim quality, suggesting that meritorious claims, not weak ones, attract third-party funding. *See* MAX SCHANZENBACH & DAVID DANA, HOW WOULD THIRD PARTY FINANCING CHANGE THE FACE OF AMERICAN TORT LITIGATION? THE ROLE OF AGENCY COSTS IN THE ATTORNEY-CLIENT RELATIONSHIP (2009), *available at* http://www.law.northwestern.edu/searlecenter/papers/Schanzenbach_Agency%20Costs.pdf (paper presented at Northwestern Law School public policy roundtable on alternative litigation finance). An evaluation of the competing empirical assertions in these submissions and in the scholarly literature – e.g. that ALF tends to increase the filing of non-meritorious claims – is beyond the mandate and expertise of the Commission on Ethics 20/20, which was not intended to engage in social science research.

with respect to an ALF transaction, the duties considered in this Informational Report are applicable.

The Commission identified numerous issues upon which it sought public comment, and prepared an Issues Paper, which was made available on November 23, 2010. Comments were received until February 15, 2011. In addition, the Commission heard public testimony at the American Bar Association Midyear Meeting in Atlanta, Georgia, on February 11, 2011.

Written submissions were provided by lawyers whose clients had used ALF and entities that provide ALF to the consumer or commercial market, or that, in one case, provide loans to lawyers. In addition, there were submissions from various organizations and groups, including the American Tort Reform Association, the American Insurance Association, the Product Liability Advisory Council, and the United States Chamber of Commerce, and from Alan B. Morrison, Associate Dean for Public Interest & Public Service, George Washington University Law School.

The Commission also heard from witnesses who provided oral statements concerning ALF and answered questions posed to them by the Working Group. They were: Douglas Richmond, AON Global Profession Practice; Harvey Hirschfeld, American Litigation Finance Association (ALFA); John Beisner, Skadden Arps, on behalf of U.S. Chamber Institute for Legal Reform; and Gary Chodes, Oasis Legal Finance.

To obtain further public comments, the Commission released a draft of this Informational Report in September 2011 and received comments through November 22, 2011.

One theme of this Informational Report is that it is difficult to generalize about the ethical issues for lawyers associated with alternative litigation finance across the many differences in transaction terms, market conditions, relative bargaining power of the parties to the transactions, and type of legal services being financed. Regulation that might be appropriate for products in a sector of the market such as relatively unsophisticated one-off individual personal-injury plaintiffs, may be inappropriate in a different segment of the market, as exemplified by investments by hedge funds or high-net-worth individuals in commercial litigation. Moreover, this is a still-evolving industry, and new forms of financing may be developed that raise new concerns. Nevertheless, the Commission believes it will be helpful to the profession to consider some of the types of problems that lawyers may encounter as a result of their own, or their clients', interaction with alternative litigation finance. This Informational Report is meant as a beginning to the U.S. legal profession's conversation about ALF through the highlighting of associated ethics issues. The Commission hopes that the Association will continue and broaden this discussion by forming a body comprised of relevant and interested Association entities (e.g., the Litigation Section, Dispute Resolution Section, Section of International Law, and the Standing Committee on Ethics and Professional Responsibility) to study and develop any necessary policy proposals regarding the regulation of ALF.

II. Executive Summary

The general conclusion of this Informational Report is that lawyers must approach transactions involving alternative litigation finance with care, mindful of several core professional obligations. That said, the Informational Report should not be interpreted as suggesting that alternative litigation finance raises novel professional responsibilities, since many of the same issues discussed below may arise whenever a third party has a financial interest in the outcome of the client's litigation. A lawyer must always exercise independent professional judgment on behalf of a client,[7] and not be influenced by financial or other considerations. Moreover, a lawyer must not permit a third party to interfere with the exercise of independent professional judgment. Numerous specific provisions in the American Bar Association Model Rules of Professional Conduct ("Model Rules"), including conflicts of interest rules and rules governing third-party payments of fees, reinforce the importance of independent professional judgment.[8]

In addition, lawyers must be vigilant to prevent disclosure of information protected by Model Rule 1.6(a), and to use reasonable care to safeguard against waiver of the attorney-client privilege. Any infringement on rights that clients would otherwise have, resulting from the presence of alternative litigation finance, requires the informed consent of the client after full, candid disclosure of all of the associated risks and benefits.

Lawyers who are not experienced in dealing with these funding transactions must become fully informed about the legal risks and benefits of these transactions, in order to provide competent advice to clients. Because this is a new and highly specialized area of finance, it may be necessary for a lawyer to undertake additional study or associate with experienced counsel when advising clients who are entering into these transactions.

III. Overview of Alternative Litigation Finance (ALF)

All litigation, even *pro se* litigation, requires some degree of monetary funding. Most entity clients, at least on the defendants' side, pay on an ongoing basis for the work of their lawyers, out of their operating budgets or from existing sources of credit. This is true whether the client itself is paying for litigation expenses or the expenses are paid by its insurer under the contractual obligations of a liability insurance policy. However, certain plaintiffs' claims, particularly individual personal injury tort claims, are funded by the plaintiff's lawyer advancing the value of the lawyer's time, and sometimes also the expenses of litigation to the client. These advances are subsequently repaid out of the proceeds of a judgment or settlement, if the claim is

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[7] *See* MODEL RULES OF PROF'L CONDUCT R. 2.1 (2011) [hereinafter MODEL RULE XX]; MODEL RULES PROF'L CONDUCT ANN. 286 (7th ed. 2011).

[8] *See* MODEL RULE 1.7(a)(2) (representation materially limited by lawyer's responsibilities to a third party or the lawyer's own interests); MODEL RULE 1.8(e) (with limited exceptions, lawyers may not provide financial assistance to client); MODEL RULE 1.8(f) (lawyer must not accept compensation for representation from third party without informed consent of client and unless it will not interfere with independent professional judgment); MODEL RULE 1.8(i) (lawyers may not acquire proprietary interest in subject matter of representation); MODEL RULE 5.4(c) (lawyer may not permit fee payor to direct or regulate lawyer's professional judgment).

successful, pursuant to the terms of the contingency fee agreement entered into between the lawyer and client.

In some cases, however, litigants are unable to finance the cost of legal services from their operating budgets or existing lines of credit, or would prefer to access different sources of capital to finance their lawyers' bills. This may be the case for both plaintiffs and defendants, generally in large, complex, litigated matters. In addition, some litigants find themselves in urgent need of funds to pay living or medical expenses as they are accrued. Individual plaintiffs in tort actions may find themselves in this predicament.[9] They may not have access to other sources of capital, such as bank loans or credit cards, and may discover that the most valuable asset against which they can obtain capital is a contingent share in an eventual judgment or settlement. Thus, while these transactions are not intended to fund litigation expenses, they are occasioned by an injury that is the subject of ongoing litigation, and the cause of action arising out of the injury is used as security for the funding.

Following the suggestion in Steven Garber's 2009 RAND paper,[10] this Informational Report has adopted the term "alternative litigation finance" ("ALF") to describe the universe of contracts that is the subject of the paper. Defined most generally, ALF refers to mechanisms that give a third party (other than the lawyer in the case) a financial stake in the outcome of the case in exchange for money paid to a party in the case. Sometimes the money paid to the party is used to pay litigation expenses, and sometimes the money is used by the party to pay for non-litigation related expenses, such as living expenses (e.g., where the party is an individual involved in a personal injury suit). Individuals or organizations that provide capital used to support litigation-related activities, or to support clients' ordinary living expenses during the pendency of litigation, are referred to here as ALF suppliers.[11] There is a spectrum of transactions by ALF suppliers that ranges, for example, from sophisticated investments in major cases such as critical patent litigation, with the investors seeking returns akin to venture capital returns, to support of personal injury litigation. Both plaintiffs and defendants can make use of ALF, although as discussed below, the market is segmented to some extent according to the sophistication of clients/borrowers. ALF is presently characterized by spreading the risk of litigation to investors via various methods, including, predominately, nonrecourse or limited recourse financing.

ALF is relatively new in the United States but appears to be evolving as a method of providing financial support to litigants. It often takes the form of nonrecourse financing between

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[9] For example, the plaintiff in *Echeverria v. Lindner*, No. 018666/2002, 2005 WL 1083704 (N.Y. Sup. Ct. Mar. 2, 2005), was an undocumented worker injured in a construction-site accident. In order to pay for necessary back surgery, he sold a share of his personal-injury claim to a company called LawCash for $25,000, or borrowed $25,000 from LawCash – whether to construe the transaction as a loan or a sale was one of the issues considered by the court.

[10] *See* STEVEN GARBER, RAND INST. FOR CIVIL JUSTICE LAW, FIN., AND CAPITAL MKTS. PROGRAM, ALTERNATIVE LITIGATION FINANCING IN THE UNITED STATES: ISSUES, KNOWNS, AND UNKNOWNS (2010) (Occasional Paper series).

[11] Compare the definition in GARBER, *supra* note 10, at 7. For an excellent overview of the different types of ALF that parallels Garber's, *see* Jonathan T. Molot, *Litigation Finance: A Market Solution to a Procedural Problem*, 99 GEO. L.J. 65, 92-101 (2010).

two laypersons, secured solely by a claim, but it can also include loans to lawyers in a contingency fee case. Investors, both traditional and nontraditional financers, provide funding either as a lump sum or as periodic payments to a claimant in exchange for a share of the proceeds of the judgment on, or settlement of, the financed claim. The business model requires that the ALF supplier assume the risk that if the claim is unsuccessful, in whole or in part, the ALF supplier may not recover any or a part of the sums so advanced. A variation of ALF may be an investor's acquisition of a full or partial interest in a claim where the investor becomes one of the parties in interest. Information obtained by the Commission Working Group shows that, at present, investors in ALF are primarily financing the claimant, though defense side financing is also possible.[12] Funding on the defense side obviously does not involve taking a percentage interest in the claim, but often does involve the ALF supplier taking all or a percentage interest in the liability facing the defendant. As discussed below, ALF transactions between large law firms and defendants are generally negotiated individually between the parties, with the method of calculating the supplier's payment being one of the most important terms in the contract.

A. A Typology of ALF

The ALF market is apparently fairly strongly differentiated. A large number of ALF suppliers serve the consumer sector, marketing to personal-injury plaintiffs, and to other individual clients with relatively small legal claims. Consumer ALF suppliers are distinguishable from settlement factoring companies; the former take a partial assignment in a claim that has not yet been settled or reduced to judgment, while the latter purchases a claim that has been reduced to judgment, typically as a result of a judicially approved settlement. A considerably smaller number of entities fund large, complex commercial litigation. These companies conduct extensive due diligence on individual cases and make sizeable financial investments. Finally, commercial lenders and some specialized ALF companies make loans directly to lawyers, as opposed to purchasing claims or parts of claims from clients.

1. Consumer Legal Funding.

The sector of the ALF industry that has attracted the most attention, in both the popular media and in scholarly commentary, is that which provides money to consumers with pending lawsuits, most often personal-injury claims but including other individual-client causes of action such as employment discrimination and securities fraud,[13] who are generally already represented by counsel. For the purposes of this discussion, it will be assumed that the transaction involves a tort plaintiff represented by a lawyer pursuant to a standard contingency fee agreement. In a typical transaction, the ALF supplier agrees to pay a given amount of money to the plaintiff (say, $25,000) in exchange for a promise by the plaintiff to pay the ALF supplier that amount plus an additional amount (sometimes referred to as a "fee") specified in the contract in the event of a

[12] *See, e.g.*, Comments of Burford Group to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. 4 (Feb. 15, 2011) (on file with author) ("Burford is willing to finance plaintiffs and defendants with equanimity."); Comments of Juridica Capital Mgmt. Ltd. to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. 2 (Feb. 17, 2011) (on file with author) ("To date we have been involved mainly in claims by plaintiffs in major commercial litigation but we – and we understand at least one of our peers – are working on products for defendants as well.").

[13] *See* Barksdale, *supra* note 4, at 715.

positive outcome in the suit (that is, a judgment or settlement).[14] As Steven Garber's RAND Report notes, "[t]hese financing fees seem typically to increase with the elapsed time from the provision of the funds to the date on which the consumer pays the supplier, but the contracted fees do not depend on the total recovery in the underlying lawsuit or the amount of the recovery received by the consumer plaintiff."[15] The transactions are also nonrecourse, meaning that if the plaintiff recovers nothing by way of judgment or settlement, the plaintiff has no obligation to repay the amount to the supplier.

Comments received by the Working Group from entities in the ALF industry indicate that the purpose of these transactions is generally to provide funds for living expenses during the pendency of litigation.[16] Injured plaintiffs are often disabled or at least unable to work at their previous job, and may lack access to conventional sources of capital, such as bank loans and credit cards. They may therefore have a pressing need to make mortgage or rent payments, or to pay medical expenses. On the other hand, some plaintiffs may not have an urgent need for funds, but may instead be interested in monetizing the contingent value of their legal claim.[17]

In some cases lawyers will be involved in the process of negotiating a consumer-sector ALF transaction, but in other cases the client – either prior to or subsequent to the beginning of the representation – will obtain financing without the involvement of the lawyer.[18] Because this Informational Report focuses on the duties of lawyers when representing clients in connection with ALF transactions, analysis relating to consumer protection is beyond its scope. Many ALF suppliers in the consumer sector advertise to generate customers.[19] A person with a cause of action may respond to these advertisements and approach an ALF supplier without the knowledge of a lawyer. In some cases, if the claimant is already represented by counsel, a lawyer may be involved in the process of obtaining financing, in which case the duties discussed in this Informational Report are applicable. Other problems that may arise in connection with consumer ALF transactions, however, such as misleading advertising, inadequate disclosure of financing terms, and excessive financing charges, do not fall within the client-lawyer relationship and are therefore best addressed by legislation or regulation apart from the regulation of the legal

[14] Some ALF suppliers in the consumer sector made their contracts available to the Working Group. *See, e.g.*, Oasis (Nebraska) Form Purchase Agreement. Other information concerning transaction terms and the interaction between ALF suppliers and lawyers was gleaned from judicial decisions and media reports.

[15] GARBER, *supra* note 10, at 9.

[16] *See, e.g.*, Comments of Oasis Legal Finance/Alliance for Responsible Consumer Legal Funding to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. (Apr. 5, 2011) (on file with author) (indicating that purpose of consumer-sector ALF is to "enable these consumers to pursue their legal claims without worrying about how they are going to pay for basic living expenses").

[17] *See* GARBER, *supra* note 10, at 10.

[18] *See, e.g.*, *Fausone v. U.S. Claims, Inc.*, 915 So.2d 626, 627-28 (Fla. Dist. Ct. App. 2005), *aff'd*, 931 So. 2d 899 (Fla. 2006) ("In fairness to U.S. Claims, it should be emphasized that there is no evidence that it solicited Ms. Fausone. How or why she contacted them is not contained in the record.").

[19] *See* GARBER, *supra* note 10, at 12. As Garber notes, running a Google search using terms like "lawsuit cash" or "litigation funding" generates pages of hits, with links to websites with names like LawMax Legal Finance, My Legal Advance, Fast Funds, LawCash, CaeCah, Legal Advance Funding, Funding Cash, LawLeaf, and Advance Cash and Settlement Funding.

profession.[20]

2. Investing in Commercial Litigation

A very different segment of the ALF market involves public and private funds that seek to invest in large, complex commercial lawsuits, including contract, intellectual property, and antitrust litigation. Two public companies in this industry, Juridica and Burford, primarily invest in claims owned by large corporate litigants represented by major law firms; their investments are reportedly in the range of $500,000 - $15 million.[21] Other funds are private and therefore less is known about the nature and scope of their investments.

The terms of agreements between suppliers in this sector and recipients of funding are generally confidential. When these contracts have been publicly disclosed, they appear to be "bespoke" documents negotiated between the recipient of funding and the ALF supplier, as opposed to the standard-form contracts employed in the consumer funding sector.[22] Many users of ALF in this sector of the market are sophisticated, repeat-player litigants, generally with in-house legal representation. Thus, it is likely that lawyers have been involved in the process of negotiating the terms of the agreement.

3. Loans to Lawyers and Law Firms

Commercial lenders and some specialized ALF suppliers provide loans or lines of credit directly to law firms. These loans are typically secured by assets of the firm, such as furniture and fixtures, the firm's accounts receivable, or the firm's contingent interests in ongoing cases.[23] As two Canadian lawyers noted, regarding the difficulty of funding complex litigation:

> We suspect it is very difficult for most Canadian counsel to wrap their minds around the concept of financing $2.6 million of disbursements. How many of us can claim an "Uncle Pete" relationship with our bankers that will support a million dollar loan to finance a single case? How many of us can finance the balance of $1.6 million from our "war chest" left over from our successful cases?[24]

A similar problem, of finding funds to pay for millions of dollars in disbursements, faces lawyers in the United States as well. Law firms representing plaintiffs and defendants may seek financing to support ongoing expenses of litigation. It may be the case, however, that firms representing plaintiffs are more likely to make use of nontraditional lenders as a source of

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[20] The Commission and its Working Group did not attempt a comprehensive review of existing statutes and regulations concerning ALF, but there are a handful of recently adopted state laws concerning the relationship between ALF providers and citizens in those states. This is a subject that could be addressed by the ABA as part of the broader discussion referenced at page 3 above.

[21] *Id*. at 12. *See also* Lyon, *supra* note 4, at 574 (reporting that "corporate litigants may now routinely borrow up to $15,000,000, on cases valued at $100,000,000 or more").

[22] *See, e.g.*, Parloff, *supra* note 2 (discussion of the contract between the Ecuadorian plaintiffs and Burford).

[23] GARBER, *supra* note 10, at 13.

[24] JAMES H. MACMASTER & WARD K. BRANCH, FINANCING CLASS ACTIONS 2 (2002), *available at* http://www.branchmacmaster.com/storage/articles/classactions_financing.pdf.

financing.[25]

B. Common-Law Doctrines Historically Affecting ALF

1. Maintenance and Champerty

Maintenance, champerty and barratry are closely related but are not identical. "[P]ut simply, maintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty.'"[26]

a. Historical Background.

Champerty is considered a type of maintenance. The historical justification for prohibiting any form of maintenance was that third-party funding of litigation encouraged fraudulent lawsuits. The wealthy and powerful would "buy up claims, and, by means of their exalted and influential positions, overawe the courts, secure unjust and unmerited judgments, and oppress those against whom their anger might be directed."[27] As one contemporary scholar put it, "[b]arons abused the law to their own ends and . . . bribery, corruption, and intimidation of judges and justices of the peace [was] widespread."[28] Whether this historical analysis was accurate or not, American courts long ago held that the risk that courts could be easily bribed or corrupted by third parties had disappeared with the advent of then modern reforms.[29]

Furthermore, the modern doctrines of abuse of process, malicious prosecution, and wrongful initiation of litigation deal more directly with the problems that may have originally motivated the common law doctrine of champerty, since they provide victims of third-party interference a remedy when a third party promotes litigation that is based on fraudulent allegations or baseless legal theories.[30] Given that existing ethical and legal obligations of lawyers and their clients are already supposed to insure that litigation be conducted in good faith and non-frivolously, it is unclear why the historical concerns of the common law would justify today placing special burdens on litigation funded by third parties.

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[25] GARBER, *supra* note 10, at 13.

[26] *Osprey, Inc. v. Cabana Ltd. P'ship*, 532 S.E.2d 269, 273 (S.C. 2000) (*quoting In re Primus*, 436 U.S. 412, 424 n.15 (1978)).

[27] *Casserleigh v. Wood*, 59 P. 1024, 1026 (Colo. Ct. App. 1900).

[28] Damian Reichel, Note, *The Law of Maintenance and Champerty and the Assignment of Choses in Action*, 10 SYDNEY L. REV. 166, 166 (1983).

[29] *See, e.g. Thallhimer v. Brinckerhoff*, 3 Cow. 623 (N.Y. Sup. Ct. 1824) ("In modern times, and since England has enjoyed a pure and firm administration of justice, these evils are little felt, and champerty and maintenance are now seldom mentioned . . . as producing mischief in that country.").

[30] *See Sec. Underground Storage, Inc. v. Anderson*, 347 F.2d 964, 969 (10th Cir. 1965) (explaining that the common law of champerty has been replaced by modern remedies such as abuse of process, malicious prosecution and wrongful initiation of litigation). Although the common law's purpose in attacking maintenance and champerty has been analogized to the purpose now served by the tort of malicious prosecution, differences remain, such as the fact that malicious prosecution requires proof of malice or the lack of probable cause, whereas an allegation of maintenance required only proof that the suit supported was groundless. *See Weigel Broad. Co. v. Topel*, 1985 U.S. Dist. LEXIS 23862 (N.D. Ill. Aug. 19, 1985) at *18.

Limitations on maintenance can come from two sources: common law and statutes. There are currently two states with statutes that follow the early English common law's approach and prohibit any form of maintenance (even maintenance that is not for profit). Here, for example, is Mississippi's law:

> It shall be unlawful for any person . . . either before or after proceedings commenced: (a) to promise, give, or offer, or to conspire or agree to promise, give, or offer, (b) to receive or accept, or to agree or conspire to receive or accept, (c) to solicit, request, or donate, any money . . . or any other thing of value, or any other assistance as an inducement to any person to commence or to prosecute further, or for the purpose of assisting such person to commence or prosecute further, any proceeding in any court or before any administrative board or other agency.[31]

This language would, in theory, prohibit one neighbor from gratuitously providing something of value (information, law books, etc.) to another in connection with litigation. American common law restrictions on maintenance, in those states where they were recognized, refused to follow early English common law and were limited to restricting champerty.

In the early Twentieth Century some courts interpreted the principle of maintenance to permit third-party support only under the narrowest of circumstances. In *In re Gilman's Administratrix*, 167 N.E. 437 (N.Y. 1929), Judge Cardozo said that "maintenance inspired by charity or benevolence" could be legal but not "maintenance for spite or envy or the promise or hope of gain."[32] Gilman itself involved maintenance by the party's own lawyer, which may have made it especially obnoxious to Cardozo. This, of course, would be permitted today in every jurisdiction under the practice of the contingency fee, which had, by the mid-1930's, become generally accepted as industrialization brought more and more claims in need of legal representation.[33] It is worth noting that 65 years later the New York Court of Appeals held that an offer by a personal injury litigant to give another party 15% of his net recovery from his lawsuit in exchange for certain personal services could constitute an "enforceable assignment of funds" that created a lien on the proceeds of the lawsuit.[34]

Other courts in the same period took a broader view of maintenance in cases involving a third party who was not the party's own lawyer. These courts came to view maintenance between two laypersons as permissible regardless of whether it was done for charity or profit, or

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[31] MISS. CODE ANN. § 97–9–11 (2009). Illinois' law sweeps slightly less broadly:

> If a person officiously intermeddles in an action that in no way belongs to or concerns that person, by maintaining or assisting either party, with money or otherwise, to prosecute or defend the action, with a view to promote litigation, he or she is guilty of maintenance and upon conviction shall be fined and punished as in cases of common barratry. It is not maintenance for a person to maintain the action of his or her relative or servant, or a poor person out of charity.

720 ILL. COMP. STAT. 5/32–12 (2009). Illinois allows selfless maintenance when the recipient of the support is either one's family or a person who is poor.

[32] *In re Gilman's Administratrix*, 167 N.E. at 440.

[33] *See* Max Radin, *Maintenance By Champerty*, 24 CAL. L. REV. 48, 70-71 (1936). *See also* Richard W. Painter, *Litigating on a Contingency: A Monopoly of Champions or a Market for Champerty?*, 71 CHI.-KENT L. REV. 625, 639–40 (1995) (discussing how contingent fees were eventually excepted from the doctrine of champerty).

[34] *See Leon v. Martinez*, 638 N.E.2d 511, 514 (N.Y. 1994).

whether the supplier was the client's lawyer or a stranger.[35]

b. Contemporary Views.

As the Ninth Circuit Court of Appeals stated in 2011, "[t]he consistent trend across the country is toward limiting, not expanding," the common law prohibition of champerty.[36] In some states, such as Arizona, California, Connecticut, New Jersey, New Hampshire, New Mexico and Texas, the courts have held that the early common law prohibitions on champerty were never adopted from England.[37] In other states, such as Colorado, champerty laws, if they had been adopted from England, were later abandoned.[38] The Massachusetts Supreme Judicial Court struck down Massachusetts' champerty laws in 1997. The court stated that "the decline of champerty, maintenance, and barratry as offences [sic] is symptomatic of a fundamental change in society's view of litigation – from 'a social ill, which, like other disputes and quarrels, should be minimized,' to 'a socially useful way to resolve disputes.'"[39] In Florida, the common law prohibition of champerty was discarded by an appellate court, which held in a case involving litigation funding that no claim of champerty exists unless a stranger to a lawsuit "officiously intermeddles" in the suit.[40] In New York, the *Leon* case cited above established that the courts would enforce the partial assignment of the proceeds of a lawsuit resulting from an exchange of the assignment for something of value, such as services (in that case, home health care).[41]

According to the one recent survey on the topic, 27 out of 51 jurisdictions, including the District of Columbia, permit some form of champerty, subject to the sort of limits described as follows.[42] In these jurisdictions champerty is generally permissible as long as the supplier is not:

(1) clearly promoting "frivolous" litigation (e.g. a lawsuit that does vindicate a genuine legal interest of the party bringing the suit);

(2) engaging in "malice champerty", which is the support of meritorious litigation motivated by an improper motive. (e.g. prima facie tort in NY);

(3) "intermeddling" with the conduct of the litigation (e.g. determining trial strategy or controlling settlement).

Given paucity of modern cases that directly discuss the kind of transactions that comprise

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[35] *See, e.g., L. D. Brown v. John Bigne et al.*, 28 P. 11 (Ore. 1891).
[36] *Del Webb Cmtys., Inc. v. Partington*, 652 F.3d 1145, 1156 (9th Cir. 2011).
[37] *In re Cohen's Estate*, 152 P.2d 485 (Cal. Dist. Ct. App. 1944); *Polo by Shipley v. Gotchel*, 542 A.2d 947 (N.J. Super. Ct. Law Div. 1987); *Anglo-Dutch Petroleum Int'l, Inc. v. Haskell*, 193 S.W.3d 87, 103–04 (Tex. App. 2006).
[38] *Fastenau v. Engel*, 240 P.2d 1173 (Colo. 1952) ("Common-law maintenance and champerty no longer exist in Colorado.").
[39] *Saladini v. Righellis*, 687 N.E.2d 1224, 1226 (Mass. 1997). *See also Osprey, Inc. v. Cabana Ltd. P'ship*, 532 S.E.2d 269, 273 (S.C. 2000) (abolishing champerty under South Carolina law).
[40] Officious intermeddling means "offering unnecessary and unwanted advice or services; meddlesome, esp. in a highhanded or overbearing way." Mere provision of financing to a plaintiff is not enough. *Kraft v. Mason*, 668 So. 2d 679, 682 (Fla. Dist. Ct. App. 1996).
[41] *Leon v. Martinez*, 638 N.E.2d 511 (N.Y. 1994).
[42] Sebok, *supra* note 4, at 98-99.

ALF as discussed in this Informational Report, there may be more states in which champerty is tolerated or where, if the issue were raised again in a modern context, a contemporary court would have little reason to preserve the doctrine of maintenance, either as a matter of common law or public policy. Some states have recently reversed the common law prohibition of champerty through legislation.[43] However, other states have reaffirmed these doctrines through the courts, noting "the potential ill effects that a champertous agreement can have on the legal system."[44]

2. Usury

Usury is the taking of interest at a rate that exceeds the maximum rate provided by law for the particular category of lender involved in the transaction. There is considerable variation from state to state in the interest rates that constitute usury and in the extent to which different rates may be specified for different types of lenders (e.g., banks, insurance companies, merchants, etc.).

Discussions of ALF often refer to the funding provided as a loan.[45] ALF suppliers, on the other hand, assert that they are making an investment or purchasing a share of a claim, not making a loan.[46] Whether these transactions are characterized as a loan or an investment may determine whether state usury provisions apply to the rate of return specified in the contract.

Generally speaking, debt, at least in the context of consumer usury law, involves a transaction in which the borrower has an absolute obligation to repay the sum advanced.[47] Some

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[43] *See, e.g.*, ME. REV. STAT. ANN. tit. 9–A, §§ 12–101 to –107 (2009) (partially amending ME. REV. STAT. ANN. tit. 17–A, § 516(1) (2009)); OHIO REV. CODE ANN. § 1349.55 (West 2009) (superseding *Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217 (Ohio 2003)).

[44] *Johnson v. Wright*, 682 N.W.2d 671, 680 (Minn. Ct. App. 2004)*; see Wilson v. Harris*, 688 So.2d 265, 270 (Ala. Civ. App. 1996), *quoting Lott v. Kees*, 165 So. 2d 106 (Ala. 1964) ("The doctrine of champerty is directed against speculation in lawsuits and to repress the gambling propensity of buying up doubtful claims."). In dicta another court speculated that a rate of return disproportionate to the investor's risk might render the contract voidable for unconscionability. *Fausone v. U.S. Claims, Inc*., 915 So.2d 626, 630 (Fla. Dist. Ct. App. 2005), *aff'd*, 931 So.2d 899 (Fla. 2006). On the record before the court, however, no findings were possible concerning the risk of non-recovery.

[45] *See, e.g.*, N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 2011-2 (2011) ("This opinion addresses non-recourse litigation loans, *i.e.* financing repaid by a litigant only in the event he or she settles the case or is awarded a judgment upon completion of the litigation.").

[46] *See, e.g.*, Comments of Augusta Capital, LLC to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. (Feb. 7, 2011) (on file with author) ("The funding that Augusta Capital provides is entirely contingent - the lawyer is not obligated to repay any portion of the funding provided by Augusta Capital - nor to pay any fee to Augusta for the funding - for a particular case unless and until a recovery is made in that particular case."); Comments of Oasis Legal Finance, LLC to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. (Jan. 18, 2011) (on file with author) ("This product does not fall into a traditional 'loan product' category as it is non-recourse.").

[47] *See Odell v. Legal Bucks, LLC*, 665 S.E.2d 767, 777 (N.C. Ct. App. 2008) (citations omitted) ("[A] transaction in which the borrower's repayment of the principal is subject to a contingency is not considered a loan because the terms of the transaction do not necessarily require that the borrower repay the sum lent or return a sum equivalent to that which he borrow[ed]."); 1-6 CONSUMER CREDIT LAW MANUAL § 6.08 (2011) ("The second element of a traditional usury case is the debtor's absolute obligation to repay the principal amount of the money transferred to him or her."); Cynthia Bulan, *A Small Question in the Big Statute: Does Section 402 of Sarbanes-Oxley Prohibit Defense Advancements?*, 39 CREIGHTON L. REV. 357, 374-75 (2006) ("A handful of courts have addressed the

courts have relied upon this understanding of the definition of debt to state that ALF is not lending.[48] However, some may argue that notwithstanding the absence of any judicial precedent applicable to ALF, such advances from a supplier are in reality "nonrecourse loans." Consistent with this perspective, some courts have characterized ALF transactions as loans, potentially triggering state law usury limitations.[49] In 2010, two of the major national consumer-sector ALF providers sued the Colorado Attorney General to obtain a declaratory judgment holding that their activities are not loans and are not in violation of Colorado's Uniform Consumer Credit Code. Recently, the trial judge hearing this suit held that under Colorado's Uniform Consumer Credit Code, debt need not be recourse and therefore consumer ALF transactions made with an "expectation of repayment" may not charge more than the interest rate set by that state's usury law.

C. Examples of ALF Transactions

The following hypothetical scenarios illustrate some of the ways in which lawyers may be involved when they represent clients receiving funds from ALF suppliers. The hypotheticals also suggest some of the ethical issues confronting lawyers.

Case 1: Plaintiff was injured in a car accident and his injuries have rendered him unable to perform his job involving physical labor at a factory. Plaintiff has many financial obligations, including rent payments and other bills coming due, but is unable to borrow money from traditional lenders or to take out further cash advances on his credit card. Lawyer is a personal injury lawyer representing Plaintiff in the accident litigation. Lawyer believes Plaintiff's case has a reasonable likelihood of settling for $100,000, but due to a slow state court docket, Lawyer expects it will take 18 months or more to settle the case. Plaintiff tells Lawyer that he has seen late-night television ads run by Supplier offering "cash for lawsuits," and asks Lawyer whether he should sell a portion of his claim to Supplier. Lawyer is unfamiliar with the terms of the financing contracts entered into between Supplier and its customers. How should Lawyer advise Plaintiff?

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definition of 'loan' . . . . [I]t appears that the large majority of courts, both federal and state, that have considered the issue have held that an advancement of funds that comes with only a conditional obligation to repay would not constitute a 'loan'").

[48] *See, e.g.*, *Dopp v. Yari*, 927 F. Supp. 814 (D.N.J. 1996); *Kraft v. Mason*, 668 So. 2d 679 (Fla. Dist. Ct. App. 1996); *Nyquist v. Nyquist*, 841 P.2d 515 (Mont. 1992); *Anglo-Dutch Petroleum Int'l, Inc. v. Haskell*, 193 S.W.3d 87, 96 (Tex. Ct. App. 2006).

[49] *See, e.g.*, *Lawsuit Financial, LLC v. Curry*, 683 N.W.2d 233 (Mich. Ct. App. 2004); *Echeverria v. Estate of Lindner*, No. 018666/2002, 2005 WL 1083704 (N.Y. Sup. Ct. Mar. 2, 2005). The same ALF contract that was at issue in *Echeverria* (where the ALF supplier, not being a party, did not have the opportunity to brief the court on New York law), was later declared to be valid and not covered by New York's usury statutes in a suit for declaratory judgment brought by the ALF supplier. Plaintiff Funding Corporation d/b/a LawCash v. Echeverria, No. 10140/2005 (N.Y. Sup. Ct. 2005). In Ohio, the lower courts in the *Rancman* case characterized an ALF transaction as a loan, but the Ohio Supreme Court invalidated the contract with the supplier on a different ground, concluding that it violated state law prohibitions on champerty. *See Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217 (Ohio 2003). The Ohio legislature subsequently overruled *Rancman* and permitted transactions of the sort involved in that case. In North Carolina, the Court of Appeals held that, although the ALF supplier had not provided a loan for the reasons explained *supra*, it had provided an "advance," which did fall under North Carolina's usury statute, even though an advance was not a loan. *Odell v. Legal Bucks, LLC*, 665 S.E.2d 767, 778 (N.C. Ct. App. 2008).

Variation: Lawyer has represented personal-injury clients in other cases who have sold portions of their claims to Supplier. Based on this experience Lawyer knows that Supplier does not request to inspect confidential documents, but relies for its due diligence on filed pleadings and other publicly available information. Lawyer also reasonably believes that Supplier clearly discloses the terms of the financing contract with its customers. Based on other agreements Lawyer has seen between Supplier and its customers, Lawyer reasonably believes that Supplier will not require Plaintiff to agree to convey any decision-making authority with respect to the representation to Supplier.

Case 2: Plaintiff enters into a contract with a funding company, Supplier, which advertises extensively with slogans such as "quick cash today!" The contract terms provide that, in exchange for $25,000, Plaintiff agrees to repay Supplier the principal amount of $25,000 plus financing charges computed at a monthly rate of 3.85% of the principal amount, compounded monthly, plus various charges denominated "case review" and "case servicing" fees. The obligation to repay Supplier has priority over Plaintiff receiving any proceeds from a settlement or judgment in the litigation, and Plaintiff and Plaintiff's lawyer are required to hold any proceeds in trust until the obligation to repay Supplier has been satisfied. In addition, under the agreement Plaintiff permits Supplier to inspect any pleadings, reports, memoranda or other documents relating to the lawsuit, and agrees to waive any duty of confidentiality that would restrict Plaintiff's lawyer from disclosing this information to Supplier. Plaintiff also agrees to prosecute the lawsuit vigorously and in good faith, and to give Supplier notice of any termination or substitution of counsel. Finally, Plaintiff agrees not to accept any offer of settlement without giving written notice to Supplier and obtaining Supplier's consent to the settlement.

Plaintiff has retained Lawyer to represent him in a personal-injury lawsuit. After Plaintiff and Lawyer signed a retention agreement, Plaintiff told Lawyer about the contract with Supplier. After reviewing the contract, Lawyer became concerned about her ability to represent Plaintiff effectively. What should Lawyer do now?

Case 3: Plaintiff, an inventor, approaches Lawyer, an intellectual property lawyer, about pursuing a patent infringement action against a large manufacturing company. The matter will be complex and likely take several years to complete, and the prospective defendant is notorious for using delaying tactics to drive up the litigation costs of its adversaries. Lawyer does not have sufficient capital on hand to represent Plaintiff on a contingent fee basis. Lawyer therefore recommends that Plaintiff approach Supplier, a company that buys shares in causes of action asserted in complex commercial disputes. Lawyer has dealt with Supplier in the past in connection with the representation of other clients, but does not receive compensation for referring clients to Supplier.

In the course of negotiating the agreement between Plaintiff and Supplier, numerous issues have arisen. Supplier has insisted that its claim have priority in the proceeds of any judgment or settlement recovered, so that Plaintiff does not receive anything until Supplier is paid in full. That is, Supplier would get paid after Lawyer, but before Plaintiff. Supplier also seeks unrestricted access to all documents in Lawyer's possession, including those that may be

protected by the attorney-client privilege or work product doctrine. Supplier asks Lawyer to agree not to withdraw or associate with co-counsel without the express written consent of Supplier. Finally, Supplier proposed a contract term requiring Plaintiff to seek Supplier's agreement before accepting any offer of settlement.

How should Lawyer proceed in the negotiations with Supplier on behalf of Plaintiff?

Case 4: Lawyer is a personal-injury attorney specializing in class action and non-class aggregate litigation. Product liability lawsuits have recently been filed against a pharmaceutical company, asserting that the manufacturer knew but failed to warn of dangerous side effects of a prescription drug. Lawyer believes it would be possible to attract numerous clients with potential claims against the manufacturer, but is concerned that the litigation will be lengthy, vigorously contested by the manufacturer, and therefore expensive. Lawyer does not have sufficient capital on hand in her firm's account to finance the case herself, with the aim of recouping the expenses through a contingency fee obtained after a judgment or settlement. Lawyer therefore approaches a commercial lender about establishing a line of credit to be used for the purpose of financing the case. The lender agrees to make a loan, secured by Lawyer's office fixtures and accounts receivable. The interest rate is at fair market value for this type of loan. Lawyer subsequently is retained by hundreds of clients in a non-class aggregate lawsuit against the manufacturer. The clients agree to pay Lawyer one-third of the amount of any judgment or settlement received, plus expenses advanced by Lawyer on their behalf, and sign a contingent fee agreement that complies with Model Rule 1.5(c) except that it does not mention the possibility of borrowing funds and passing along interest expenses. After recovery is obtained for the clients, may Lawyer charge the clients a pro rata share of the borrowing costs Lawyer incurred to finance the litigation?

IV. Professional Responsibility Issues

A. Independent Professional Judgment and Conflicts of Interest

The conflicts of interest provisions in the ABA Model Rules of Professional Conduct, principally Model Rules 1.7 through 1.11, protect clients from having to assume the risk that their interests will be harmed because of the lawyer's relationship with another client, a former client, or a third party, or the lawyer's own financial or other interests. Protected interests of clients include the confidentiality of information shared with their lawyers, the reasonable expectation of loyalty of counsel, and the interest in receiving candid, unbiased advice. Conflicts rules regulate prophylactically, prohibiting lawyers from representing clients while subject to a conflict of interest, without obtaining the informed consent of their clients (where permitted). In a sense the conflicts rules provide a second layer of protection, beyond rules directly regulating conduct such as the disclosure of confidential information (Model Rule 1.6) or the exercise of independent professional judgment and the provision of candid legal advice (Model Rule 2.1).

1. Conflicts of Interest

The involvement of ALF has the potential to create conflicts of interest if the lawyer participates directly in or benefits financially from the ALF transaction, as opposed to simply advising the client in connection with the transaction.

Numerous provisions in the Model Rules of Professional Conduct regulate the conflicts of interest that may be created or exacerbated by the presence of ALF. In addition to the general material-limitation conflicts rule (Model Rule 1.7(a)(2)), and the regulation of business transactions with clients (Model Rule 1.8(a)), two non-waivable conflicts rules prohibit a lawyer from providing financial assistance to a client (Model Rule 1.8(e)) and acquiring a proprietary interest in the client's cause of action (Model Rule 1.8(i)). Although it is not denominated a conflicts rule, the principles governing withdrawal from representation require that a client be free to terminate the representation without restriction. An agreement between an ALF supplier and a client, permitting the ALF supplier to have veto power over the selection of counsel, may limit the client's right to terminate counsel in a manner that is inconsistent with Model Rule 1.16(a). Finally, a separate rule governs the provision of evaluations to someone other than the client.[50]

The analysis of conflicts of interest here assumes that a client-lawyer relationship exists only between the lawyer and the client seeking the services of an ALF supplier. If the lawyer also has a professional relationship with the ALF supplier, then a conventional concurrent conflict of interest arises, which must be analyzed under the principles of Model Rule 1.7. A professional relationship with the supplier may arise by express contract or by implication from the conduct of the parties.[51] For example, in *Leon v. Martinez*, 638 N.E.2d 511 (N.Y. 1994), the New York Court of Appeals held that the allegations in the supplier's complaint were sufficient to support a cause of action for legal malpractice against the lawyer who had been representing the plaintiff in personal-injury litigation. In particular, the lawyer had performed legal services for the supplier in the past, suggesting it was permissible to infer that the lawyer had intended to represent both the plaintiff and the supplier in the funding transaction.

a. Material Limitation Conflicts: Model Rule 1.7(a)(2)

A conflict of interest under Model Rule 1.7(a)(2) may arise if a lawyer has a relationship with an ALF supplier that creates a financial interest for the lawyer that may interfere with his or her obligation to provide impartial, unbiased advise to the client. For example, an attorney may have an agreement with an ALF supplier that it will pay the lawyer a referral fee for clients who use the supplier's services. Attorneys are prohibited from paying others for referrals of clients, Model Rule 7.2(b), but there is no explicit prohibition in the Model Rules on receiving referral fees. Nevertheless, the acceptance of referral fees very likely constitutes a material limitation on the representation of the client, resulting from a personal interest of the lawyer.[52] Under Model Rule 1.7(a)(2), therefore, the lawyer would be required to obtain the informed consent of the client to the referral-fee arrangement. Even in the absence of an explicit agreement to refer

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[50] *See* MODEL RULE 2.3.

[51] *See* RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 14 (2000) [hereinafter RESTATEMENT § xx].

[52] In some jurisdictions ethics opinions state that these fees are prohibited outright, presumably because the risk that they will interfere with the lawyer's independent professional judgment is too great. *See infra* note 91.

clients, a lawyer with a long-term history of working with a particular ALF supplier may have an interest in keeping the supplier content, which would create a conflict under Rule 1.7(a)(2).

A more subtle material limitation conflict could arise from the lawyer's involvement in negotiating a contract with an ALF supplier. In Case 3, above, the lawyer representing the inventor is negotiating with the funding company, but the terms of the agreement may have an impact on the lawyer's own interests. In the case of a contract negotiation over the structure of a financing arrangement, the conflict arises because the lawyer may have incentives to act in ways that are not in the client's best interests. A conflict of interest exists if any interest of the lawyer:

> would materially impair the lawyer's ability to consider alternative courses of action that otherwise would be available to a client, to discuss all relevant aspects of the subject matter of the representation with the client, or otherwise to provide effective representation to the client.[53]

Case 3 is but one instance of a conflict of interest that can arise regardless of whether or not ALF is present. A lawyer working under a contingent fee may share with a third party who lends money to the client an interest that the litigation be resolved sooner than the client's objectively determined interests might dictate. A lawyer may be able to disregard these incentives, give the client impartial advice, and provide competent representation, and the Model Rules are designed to make it possible for a lawyer to fulfill her professional obligations in the face of such incentives. Nevertheless, the client is entitled to know about the *risks* presented by the lawyer's financial and other incentives created by the contract, and to have an opportunity to provide or decline informed consent. The risks include the possibility that some term of the agreement may adversely affect the client's financial interests relative to those of the lawyer. For example, the ABA Standing Committee on Ethics and Professional Responsibility has concluded that an attorney may acquire an ownership interest in the stock of a corporate client, but that the client must give informed consent to the investment and the transaction must satisfy the requirements of Model Rule 1.8(a).[54] The concern in these stock-for-fees transactions is that the lawyer might structure the transaction in some way that is unfair to the client. Thus, in a situation like Case 3, the lawyer must ensure that the client is adequately informed of the risk that the agreement negotiated between the lawyer and the ALF supplier may favor the lawyer's financial interest over that of the client.

As a result, the lawyer must obtain the client's informed consent, confirmed in writing, to the conflict presented by the lawyer's role in the funding contract. Informed consent means the client's agreement "after the lawyer has communicated adequate information and explanation about the material risks and reasonably available alternatives to the proposed course of conduct."[55] Thus, the lawyer in Case 3 would be required to explain to the client the ways in which the contract terms proposed by the ALF supplier could adversely affect the client's interests. For example, the schedule of payments from the proceeds of the lawsuit may be

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[53] RESTATEMENT § 125 cmt. c.

[54] ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 00-418 (2000); *see also* D.C. Bar Legal Ethics Comm., Ethics Op. 300 (2000); N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 2000-3 (2000).

[55] MODEL RULE 1.0(e).

structured in a way that favors the lawyer's interests over the interests of the client. There may be a good reason to do this – for example, it may be a way for the client to obtain the services of his or her choice of counsel – but the risks and benefits of this option must be explained fully to the client. The lawyer should also discuss reasonably available alternatives to the suggested contract terms, and suggest available alternatives to ALF funding, if they would be in the client's best interests.

Simply paying a portion of the proceeds of a judgment or settlement to an ALF supplier holding a valid lien does not create a conflict of interest.[56] A lawyer is required to deliver to a client or third party any funds in which the client or third party has an interest.[57] The *Leon* case confirms that a lawyer does not violate the obligation of undivided loyalty to a client when paying funds to a third party that the third party is entitled to receive under a valid agreement.[58] In a different case, however, the client might object to the lawyer disbursing the funds.[59] In that instance, the lawyer's obligation is stated in Model Rule 1.15(e), which requires the lawyer to hold the disputed funds separately until the dispute is resolved.[60] There may a conflict of interest under Model Rule 1.7(a)(2) if the lawyer's financial interest in obtaining a share of the disputed funds materially limits the lawyer's ability to advocate effectively for the client's rightful share of the funds; in that case, full disclosure to and informed consent by the affected client would be required.

b. Business Transactions with Clients: Model Rule 1.8(a)

A lawyer may enter into a business transaction with a client, or knowingly acquire "an ownership, possessory, security or other pecuniary interest adverse to a client" only after giving the client clearly understandable written disclosure of the terms of the transaction, along with written advice to consult independent legal counsel and a reasonable opportunity to do so, and obtaining the client's informed consent to the terms of the transaction and the lawyers role in it, in a writing signed by the client.[61] In addition, the terms of the transaction must be substantively fair and reasonable to the client.

Many ALF transactions are negotiated between the client and the supplier, with no involvement of the lawyer. Some transactions, however, are like the hypothetical described in Case 3, where the lawyer represents the client in negotiations with the ALF supplier, and where the terms of the agreement may affect the rights the lawyer and client have, *vis-à-vis* one another,

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[56] *See, e.g., Leon v. Martinez*, 638 N.E.2d 511 (N.Y. 1994).
[57] MODEL RULE 1.15(d).
[58] *See Leon v. Martinez*, 638 N.E.2d at 514.
[59] Even a requirement that the lawyer hold funds for payment to the supplier, in effect putting the lawyer in the role of escrow agent, may create a conflict of interest under Model Rule 1.7(a)(2). At common law the duty of an escrow agent is to serve as a neutral fiduciary with respect to all of the parties to the escrow. An attorney, on the other hand, may be permitted to assert non-frivolous arguments on behalf of a client that the client is entitled to disputed funds in an escrow. These differential obligations may give rise to a conflict between the attorney's role as escrow agent and as a zealous advocate for the client's interests. *See, e.g., Splash Design, Inc. v. Lee*, 103 Wash. App. 1036, 2000 WL 1772519 (Wash. Ct. App. Dec. 4, 2000).
[60] *See, e.g., Fausone v. U.S. Claims, Inc.*, 915 So. 2d 626, 629 n.4 (Fla. Dist. Ct. App. 2005) (attorney followed the procedure outline in Rule 1.15 and deposited the funds with the court until the dispute was resolved).
[61] *See* MODEL RULE 1.8(a).

in the proceeds of any recovery. Such a case likely involves the lawyer acquiring a "pecuniary interest adverse to a client," triggering the requirements of Model Rule 1.8(a). In Case 3, in addition to satisfying the requirement of obtaining informed consent to the material limitation conflict (Model Rule 1.7(a)(2)),[62] the lawyer must ensure compliance with Model Rule 1.8(a), by:

- Ensuring that the contract terms negotiated by the lawyer, respecting the interests of the lawyer, the client, and the ALF supplier, are substantively fair and reasonable from the client's point of view.
- Fully disclosing the terms of the transaction and transmitting them in writing, in terms that can be reasonably understood by the client.
- Advising the client in writing of the desirability of seeking independent legal advice, and providing a reasonable opportunity for the client to obtain separate representation in the transaction.
- Obtaining the client's informed consent, in writing, to both the substantive terms of the transaction and the lawyer's role in it (i.e. that the lawyer is also an interested party, as well as acting as the client's representative).

As discussed below (Section IV.C.2), some state bar ethics opinions have suggested that the requirements of Model Rule 1.8(a) are applicable when a lawyer obtains a loan from a commercial lender and seeks to recoup the interest expenses from clients.

c. Financial Assistance to Clients – Model Rule 1.8(e)

Model Rule 1.8(e) provides as follows:

> A lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation, except that:
>
> > (1) a lawyer may advance court costs and expenses of litigation, the repayment of which may be contingent on the outcome of the matter; and
> >
> > (2) a lawyer representing an indigent client may pay court costs and expenses of litigation on behalf of the client.[63]

The policy underlying the Rule is set out in Comment [10]: "Lawyers may not subsidize lawsuits or administrative proceedings brought on behalf of their clients, including making or guaranteeing loans to their clients for living expenses, because to do so would encourage clients to pursue lawsuits that might not otherwise be brought and because such assistance gives lawyers

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[62] *See* MODEL RULE 1.8 cmt. [3] (lawyer must comply with Model Rule 1.7 as well as Model Rule 1.8(a) when the lawyer's financial interest in the transaction "poses a significant risk that the lawyer's representation of the client will be materially limited by the lawyer's financial interest in the transaction").

[63] Limited financial assistance by lawyers to clients is permitted in the District of Columbia and Texas. *See* D.C. RULES OF PROF'L CONDUCT R. 1.8(d)(2) (2007); TEXAS DISCIPLINARY RULES OF PROF'L CONDUCT R. 1.08(d)(1) (2005).

too great a financial stake in the litigation." The Comment distinguishes prohibited financial assistance from lending court costs and litigation expenses, "because these advances are virtually indistinguishable from contingent fees and help ensure access to the courts."

The primary focus of this Informational Report is the duties of lawyers when dealing with ALF suppliers who are independent of the lawyer. When lawyers themselves become the suppliers, except through the established mechanism of contingency fee financing, this Rule may be implicated. If the Rule applies, there is no provision for waiver with the informed consent of the client. Depending on the structure of the transaction, a lawyer may also acquire an interest in the client's cause of action, which is prohibited by a separate rule, Model Rule 1.8(i).

d. Acquisition of an Interest in the Client's Cause of Action – Model Rule 1.8(i)

Model Rule 1.8(i) provides as follows:

> A lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client, except that the lawyer may:
>
> (1) acquire a lien authorized by law to secure the lawyer's fee or expenses; and
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> (2) contract with a client for a reasonable contingent fee in a civil case.

The rationale for this Rule is explained in Comment [16]. The Rule is intended primarily to reinforce the lawyer's capacity to exercise independent judgment in the representation of the client, which might be impaired if the lawyer has too great a personal interest in the representation. The Comment also notes that if the lawyer has a proprietary interest in the cause of action, the client will have a difficult time discharging the lawyer if the client is dissatisfied. The client's right to terminate the professional relationship is almost absolute (Model Rule 1.16(a)(3)), subject only to the requirement of obtaining court permission in litigated matters (Model Rule 1.16(c)).[64]

Even in states that have abolished the common law prohibition on champerty, lawyers may not engage in champertous transactions with their clients in violation of Model Rule 1.8(i). Although this Rule is grouped with other conflicts of interest rules that may be waived upon the informed consent of the client, there is no provision in Model Rule 1.8(i) for informed consent. Thus, the Rule stands as an absolute prohibition on lawyers acquiring a proprietary interest in their clients' causes of action.

Both the prohibition on acquiring an interest in the client's cause of action, Model Rule 1.8(i), and the prohibition on providing financial assistance to clients, Model Rule 1.8(e), if applied literally would call into question the propriety of contingency fee financing. Both Rules

[64] Lawyers have occasionally been permitted to assert claims for retaliatory discharge. *See* RESTATEMENT § 32 cmt. b & Reporter's Note.

therefore contain a kind of carve-out or saving clause for contingency fees.[65] Comments to Model Rule 1.8 acknowledge the similarity between prohibited transactions and contingent fees.[66] As Comment [16] notes, the prohibitions in these Rules are rooted in the common law of champerty and maintenance. Because these doctrines evolved to take account of the development of contingent-fee financing, the provisions of state rules of professional conduct preserved the distinction between prohibited assistance or acquisition of an interest in the client's cause of action, on the one hand, and permitted contingent-fee financing on the other. In substance, however, the permitted and prohibited transactions are similar – a non-party provides financial assistance to a party, or acquires an interest in the party's cause of action. Nevertheless, contingent fees are permitted, subject to the disclosure requirements of Model Rule 1.5(c).

e. Withdrawal and Substitution of Counsel

Funding agreements may purport to restrict the client's right to terminate a lawyer or to retain substitute counsel. For example, a Michigan state bar ethics opinion refers to a contract with an unnamed ALF supplier under which a tort plaintiff agrees not to terminate an existing client-lawyer relationship or substitute a different lawyer without the express written consent of the ALF supplier.[67] As between lawyer and client, the client retains the right to terminate the client-lawyer relationship at any time, with no requirement of showing good cause, subject only to the requirement of obtaining court approval if the lawyer has entered an appearance for the client in pending litigation.[68] Under principles of agency law applicable to the client-lawyer relationship, a client and lawyer cannot validly agree to a contract term that prohibits the client from discharging the lawyer.[69] Courts frequently state that the client's right to discharge a lawyer is virtually absolute.[70] Provisions in retention agreements between lawyers and clients purporting to limit the right of clients to discharge lawyers have been set aside as interfering with what should be the client's unrestricted right to terminate the relationship at any time.[71] Thus, the provision described in the Michigan opinion, in the contract between the supplier and the plaintiff, may be deemed void as a matter of public policy. In a different case, the balance of policy considerations may be different and the recipient of funding may be permitted to validly agree to limitations on rights he or she would otherwise possess. For example, while a *lawyer* is not permitted to restrict the client's right to discharge counsel, the client's contract with the supplier may restrict this right. The validity of such a provision is a matter of state law and public policy and is beyond the scope of this Informational Report.

2. Interference with Lawyers' Professional Judgment

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[65] *See* MODEL RULE 1.8(e)(1); MODEL RULE 1.8(i)(2).
[66] *See* MODEL RULE 1.8 cmts. [10], [16].
[67] *See* Mich. State Bar Standing Comm. on Prof'l Ethics, Advisory Op. RI-321 (2000); *cf. Abu-Ghazaleh v. Chaul*, 36 So. 3d 691, 693 (Fla. Dist. Ct. App. 2009) (supplier "controlled the selection of the plaintiffs' attorneys").
[68] MODEL RULE 1.16(a)(3), 1.16(c); RESTATEMENT § 32(1).
[69] *See* RESTATEMENT § 31 cmt. d.
[70] *See, e.g., Balla v. Gambro, Inc.*, 584 N.E.2d 104 (Ill. 1991) (citing the client's near-absolute right to terminate counsel as the principal reason for not recognizing a cause of action for retaliatory discharge).
[71] *See* RESTATEMENT § 32 cmt. b & Reporter's Note.

The presence of ALF has the potential to interfere with the lawyer's exercise of candid, objective, independent judgment on behalf of the client.[72] Arguably the Rules safeguarding a lawyer's independence can be seen as reinforcing the prohibition on representing a client in circumstances in which there is a significant risk that a personal interest of the lawyer will materially limit the lawyer's representation of the client.[73] Protecting professional independence is a significant rationale underlying the conflict of interest Rules.[74] Because the Model Rules treat independence in a number of separate Rules, however, it is important to consider how ALF may affect the lawyer's professional independence, and how these Rules are implicated in ALF transactions.

ALF suppliers are businesses, operated with the goal of maximizing return on investments. The investments are in legal claims, acquired in whole or in part. The interests of a supplier in any given transaction, therefore, will be to maximize the expected value of a legal claim. In order to protect their investments and to maximize the expected value of claims, suppliers may seek to exercise some measure of control over the litigation, including the identity of lawyers pursing the claims, litigation strategy to be employed, and whether to accept a settlement offer or refuse it and continue to trial. The efforts of suppliers to maximize the return on their investment may create incentives and effects that differ from what would be expected in a similar case in which ALF funding was not present.[75]

ALF suppliers may also seek the right to advise on, or even veto, decisions made by lawyers during the course of litigation. In one Florida case, for example, the supplier had the right "to approve the filing of the lawsuit; controlled the selection of the plaintiffs' attorneys; recruited fact and expert witnesses; received, reviewed and approved counsel's bills; and had the ability to veto any settlement agreements."[76] The court deemed this control sufficiently extensive to warrant treating the supplier as a "party" for the purposes of a fee-shifting statute.[77] Case 2 presents a hypothetical scenario of a client entering into a contract with an ALF supplier that obligates the client to do various things, such as permitting the supplier to inspect pleadings, waiving confidentiality, and giving the supplier a say in the hiring and firing of counsel and the decision whether to settle. While cast in extreme terms, this hypothetical raises the important and general problem of whether certain professional duties owed by lawyers to clients are non-delegable. For example, as between the lawyer and client, the client retains the authority to decide whether to settle a civil lawsuit.[78] But does it follow that the client cannot agree by

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[72] *See* MODEL RULE 2.1.

[73] *See* MODEL RULE 1.7(a)(2).

[74] *See, e.g.*, MODEL RULE 1.7 cmt. [8].

[75] *See, e.g.,. Weaver, Bennett & Bland, P.A. v. Speedy Bucks, Inc.*, 162 F. Supp. 2d 449, 451 (W.D.N.C. 2001) (alleging that a supplier keeping tabs on its investment caused a plaintiff to reject a reasonable settlement offer).

[76] *Abu-Ghazaleh v. Chaul*, 36 So.3d 691, 693 (Fla. Dist. Ct. App. 2009).

[77] It does not necessarily follow that the supplier would be deemed a "client" for other purposes, such as the application of concurrent or successive client conflicts rules. There is an extensive body of law, beyond the scope of this Informational Report, governing the formation of the attorney-client relationship. *See generally* RESTATEMENT § 14 & Reporter's Note; GEOFFREY C. HAZARD, JR., ET AL., THE LAW AND ETHICS OF LAWYERING ch. 6 (5th ed. 2010), ("Who Is the Client?").

[78] MODEL RULE 1.2(a).

contract with a third party ALF supplier to cede these rights to the ALF supplier? The fiduciary nature of the client-lawyer relationship is the reason for the unenforceability of a client-lawyer contract provision interfering with certain client rights, such as the right to make decisions respecting settlement. In an arm's-length transaction, however, these fiduciary considerations are absent. There would seem to be no reason, as a matter of contract law, to regard these contractual provisions as unenforceable, absent some facts establishing a defense such as duress or unconscionability.

Regardless of whether the provisions delegating decision-making authority to the ALF supplier would be enforceable as a matter of contract law, they may create such a limitation on an attorney's professional judgment that a reasonable lawyer might conclude that it is impossible to provide competent representation to that client. A lawyer and client may agree among themselves to limit the scope of the lawyer's duties, but these limitations must be reasonable under the circumstances (and the client must give informed consent to the limitation).[79] A contract between a would-be client and an ALF supplier may create such onerous duties on the part of the client that a lawyer would be unable to represent the client, even in a limited-scope representation. For example, a provision in a contract may permit the supplier to refuse further funding if the lawyer makes decisions in the course of the representation with which the supplier has a fundamental disagreement. The lawyer, on the other hand, has an obligation to act with reasonable competence and diligence in the representation of the client, and may reasonably believe that the funder's second-guessing of decisions made in the representation of the client is an unreasonable interference with the lawyer's professional judgment.

While it is outside the scope of this Informational Report, it should be noted briefly that state common law doctrines of champerty and maintenance may bear on the degree of control an ALF supplier is permitted to exercise over the representation.[80] Even in states permitting an ALF supplier to obtain an interest in a party's cause of action, retention by the supplier of control over the decision-making of the party and its counsel, via a contractual provision between the supplier and the party, may be deemed unlawful as champerty or maintenance.[81]

On the other hand, some ALF suppliers disclaim any control over the decision-making of lawyers, stating that they are in an entirely passive role.[82] Indeed, some reported cases note that

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[79] MODEL RULE 1.2(c).

[80] *See* Sebok, *supra* note 4, at 109-12.

[81] *See, e.g.*, *Am. Optical Co. v. Curtiss*, 56 F.R.D. 26, 29–32 (S.D.N.Y. 1971) (agreement limiting litigant's control over whether to sue violated Fed. R. Civ. P. 17(a) requirement of suit brought by real party in interest); *Kraft v. Mason*, 668 So. 2d 679, 682 (Fla. Dist. Ct. App. 1996) ("officious intermeddling" is an element of champerty); *Huber v. Johnson*, 70 N.W. 806, 808 (Minn. 1897) (voiding contract that required plaintiff to pay funder a penalty if plaintiff sued without funder's consent).

[82] *See, e.g.*, Comments of Burford Group, LLC to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. 5 (Feb. 15, 2011) (on file with author) ("Burford does not hire or fire the lawyers, direct strategy or make settlement decisions. Burford is a purely passive provider of non-recourse financing to a corporate party."); Comments of Juridica Capital Mgmt. Ltd. to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. 6 (Feb. 17, 2011) (on file with author) ("We do not seek to control any of the decisions regarding the conduct of any litigation that we finance, nor are we aware of any other supplier in this market segment who does.").

the ALF supplier exercised no control over the lawyer's representation of the client.[83]

Investments by ALF suppliers may be used for a variety of purposes, but when they are used to pay litigation expenses, an attorney must ensure that the funding arrangement does not compromise the lawyer's independent professional judgment (Model Rule 5.4(c)). Of course, interference with professional judgment is not a risk unique to ALF, but arises whenever a lawyer feels pressure to favor the interest of a non-client, regardless of whether the non-client has provided funds to pay the client's legal expenses or have some other material interest in the outcome of the client's litigation.

a. Referring Clients to ALF Suppliers

Numerous state ethics opinions have considered the issue of whether a lawyer may provide information to clients about the availability of ALF, or refer clients to ALF suppliers. The majority of these opinions conclude that it is permissible to inform clients about funding companies,[84] or to refer clients to ALF suppliers.[85] If it is legal for a client to enter into the transaction, there would appear to be no reason to prohibit lawyers from informing clients of their existence. A more difficult question is whether lawyers should evaluate the terms of the transaction for their fairness or to advise the client whether to accept the funding. As with any subject on which a lawyer offers an opinion, a lawyer should ensure his or her competence to evaluate the ALF transaction.[86] At a minimum the lawyer should become familiar with the terms of the transaction and explain its risks and benefits to the client in terms the client can understand.[87] Competent representation and reasonable communication may also require the lawyer to compare the proposed transaction with other available means of obtaining funding, and possibly to recommend alternatives. If the lawyer is not competent to evaluate the risks and benefits of the transaction, the lawyer should refer the client to a competent advisor.

Many of the state bar ethics opinions permitting referrals to ALF suppliers include qualifications, reflecting other ethical obligations owed by lawyers to their clients. Typical limitations include: Lawyers may not disclose confidential information to an ALF supplier

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[83] *See, e.g., Anglo-Dutch Petroleum Int'l, Inc. v. Haskell*, 193 S.W.3d 87, 104 (Tex. Ct. App. 2006) ("[T]here is no evidence that [the ALF suppliers] maintained any control over the Halliburton lawsuit. The agreements do not contain provisions permitting [the ALF suppliers] to select counsel, direct trial strategy, or participate in settlement discussions, nor do they permit [the ALF suppliers] to look to Anglo–Dutch's trial counsel directly for payment."). *But see Abu-Ghazaleh v. Chaul*, 36 So.3d 691, 693 (Fla. Dist. Ct. App. 2009) (ALF supplier sought right to veto any proposed settlement).

[84] *See, e.g.*, Fla. State Bar Prof'l Ethics Comm., Formal Op. 00-3 (2002); S.C. Bar Ethics Advisory Comm., Advisory Op. 94-04 (1994).

[85] *See, e.g.*, Ariz. State Bar Comm. on the Rules of Prof'l Conduct, Formal Op. 91-22 (1991); D.C. Bar Legal Ethics Comm., Ethics Op. 196 (1989); Md. State Bar Ethics Comm., Advisory Op. 89-15 (1988); Nev. State Bar Standing Comm. on Ethics and Prof'l Responsibility, Formal Op. 29 (2003); N.J. Supreme Court Advisory Comm. on Prof'l Ethics, Advisory Op. 691 (2001); N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 2011-02 (2011); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 769 (2003); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 666 (1994); Phila. Bar Ass'n Prof'l Guidance Comm., Advisory Op. 91-9 (1991).

[86] *See* MODEL RULE 1.1.

[87] *See* MODEL RULE 1.4.

without the client's informed consent;[88] lawyers should warn clients about the risk of waiver of the attorney-client privilege (often as part of obtaining informed consent to disclose confidential information);[89] lawyers may not have an ownership interest in the ALF supplier to which the client is referred;[90] lawyers may not receive referral fees or otherwise benefit financially as a result of referring the client to the ALF supplier.[91] Some opinions include the proviso that the lawyer must be satisfied that the funding arrangement is in the client's best interests,[92] which implicates the concerns, discussed in Section IV.D, below, about the lawyer's competence to make this assessment. Many opinions admonish lawyers in general terms to avoid any interference with their professional judgment as a result of involvement in the ALF transaction.[93] A South Carolina opinion even requires the lawyer to inform the ALF supplier in writing that the client, not the funding company, retains the right to control all aspects of the litigation.[94]

The prevalence of these qualifications in state bar ethics opinions shows that the interference with independent professional judgment is one of the principal perceived risks associated with ALF. The opinions also suggest, however, that this risk can be managed, by full disclosure to the client, compliance with the obligation to obtain the client's informed consent to any potential interference with a client's interests (such as confidentiality), and also awareness on the part of the lawyer of risky contract provisions.

Case 1, above, does not appear at the outset to involve any potential interference with the lawyer's professional judgment. The client has asked his lawyer whether it is advisable to sell a portion of his tort claim to an ALF supplier. In the variation on Case 1, the lawyer has acquired expertise in this area and is likely competent to advise the client on the risks and benefits of the ALF transaction. If the lawyer did not have this experience and could not evaluate the potential risks and benefits, the lawyer may honestly answer "I don't know" or, in the alternative, the lawyer might do sufficient research to be in a position to render competent legal advice to the client.[95] In either case, the ethical obligation here is primarily one of rendering competent legal

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[88] *See, e.g.*, Phila. Bar Ass'n Prof'l Guidance Comm., Advisory Op. 2003-15 (2003); Md. State Bar Ethics Comm., Advisory Op. 00-45 (2000).

[89] *See, e.g.*, Conn. State Bar Comm. on Prof'l Ethics, Informal Op. 99-42 (1999); Md. State Bar Ethics Comm., Advisory Op. 92-25 (1991); N.J. Supreme Court Advisory Comm. on Prof'l Ethics, Advisory Op. 691 (2001); N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 2011-02 (2011); Phila. Bar Ass'n Prof'l Guidance Comm., Advisory Op. 99-8 (2000).

[90] *See, e.g.*, N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 769 (2003); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 666 (1994). *Contra* Tex. Supreme Court Prof'l Ethics Comm., Advisory Op. 483 (1994) (permitting lawyer to have ownership interest in company that makes loans to the lawyer's clients); Tex. Supreme Court Prof'l Ethics Comm., Advisory Op. 465 (1991) (same).

[91] *See, e.g.*, Md. State Bar Ethics Comm., Advisory Op. 94-45 (1994); N.J. Supreme Court Advisory Comm. on Prof'l Ethics, Advisory Op. 691 (2001); N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 2011-02 (2011) (referral fee prohibited if it would compromise lawyer's independence of judgment); Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Advisory Op. 2002-2 (2002).

[92] *See, e.g.*, Fla. State Bar Prof'l Ethics Comm., Formal Op. 00-3 (2002). *Contra* Hawaii Supreme Court Disciplinary Bd., Formal Op. 34 (1994) (lawyer not required to determine whether the arrangement is fair to the client).

[93] *See, e.g.*, Md. State Bar Ethics Comm., Advisory Op. 00-45 (2000).

[94] S.C. Bar Ethics Advisory Comm., Advisory Op. 94-04 (1994).

[95] *See* MODEL RULE 1.1. See also the discussion below, Section IV.D., on the lawyer's duty of competence in advising on ALF transactions.

advice. The mere referral of the client to an ALF supplier does not implicate the lawyer's independent professional judgment.

b. Effect on Settlement

i. Express Contract Provisions

A client may agree, in a contract with an ALF supplier, to seek the consent of the ALF supplier before entering into any settlement of the client's cause of action. The Working Group reviewed numerous contracts submitted by ALF suppliers that expressly disclaim any control by the supplier over the settlement decision.[96] Nevertheless, reported cases reveal instances in which ALF suppliers have attempted to influence the decision whether or not to settle a claim.[97]

An agreement to obtain the consent of the ALF supplier to any settlement may interfere with the ability of the attorney to exercise independent professional judgment in the representation of the client. Although the decision to settle is ultimately one for the client, Model Rule 1.2(a), attorneys have a duty to provide competent advice regarding settlement, evaluating the offer from the standpoint of the client's best interests in light of the terms of the offer and the risk of proceeding with the litigation.[98] The attorney's advice should be based solely on what is best for the client, without regard to extraneous considerations such as the lawyer's interests or the interests of third parties. On the other hand, considerations of freedom of contract suggest that clients should be permitted to delegate some authority over the handling of their cases to third parties, in exchange for some valuable consideration.

As a matter of agency law, the authority to settle a claim initially belongs to the client, but the client may delegate *revocable* settlement authority to the lawyer.[99] In principle there would appear to be no reason why the client could not delegate revocable settlement authority to

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[96] For example, Oasis Legal Funding submitted its standard Nebraska purchase contract, which in a prominent disclosure states:

> **PURCHASER OASIS LEGAL FINANCE, LLC, AS THE COMPANY AGREES THAT IT SHALL HAVE NO RIGHT TO AND WILL NOT MAKE ANY DECISIONS WITH RESPECT TO THE CONDUCT OF THE UNDERLYING LEGAL CLAIM OR ANY SETTLEMENT OR RESOLUTION THEREOF AND THAT THE RIGHT TO MAKE THOSE DECISIONS REMAINS SOLELY WITH YOU AND YOUR ATTORNEY IN THE CIVIL ACTION OR CLAIM.**

Oasis Form Purchase Agreement, at 7.

[97] *See, e.g.*, *Abu-Ghazaleh v. Chaul*, 36 So. 3d 691, 694 (Fla. Dist. Ct. App. 2009) (deeming ALF supplier a "party" liable for opposing party's attorney's fees where, *inter alia*, supplier had the right to approve any settlement entered into by the recipient of funds).

[98] Although there is a split of authority, many courts hold lawyers to the general standard of reasonable care under the circumstances when advising a client whether or not to accept an offer of settlement. *See, e.g.*, *Ziegelheim v. Apollo*, 607 A.2d 1298 (N.J. 1992). The relevant "circumstances" include the inherent uncertainty involved in these decisions, but an attorney should provide the client with an informed judgment concerning the factors that go into making a decision whether to settle or proceed to trial. *See generally* 4 RONALD E. MALLEN & JEFFREY M. SMITH, LEGAL MALPRACTICE § 31:42 (2009).

[99] *See* RESTATEMENT § 22(1), (3) & cmt. c.

other agents.[100] Under general agency law principles, any delegation of authority can be revoked by the principal. The more difficult question is whether a user of ALF financing may contractually agree to make an *irrevocable* authorization to the ALF supplier to approve or reject a settlement offer. Contractual limitations on the client's authority to accept or reject settlement offers have been invalidated where the contract is between the lawyer and client.[101] As discussed in Section IV.A.2, above, as a matter of contract law a client may be able to enter into an enforceable provision in a contract with an ALF supplier, giving the supplier the right to accept or reject a proposed settlement. It is a significant open question whether that contractual delegation is such a significant limitation on the lawyer's representation of the client – because it interferes with the lawyer's exercise of independent professional judgment – that the lawyer must withdraw from the representation of a client who has agreed to such a contract provision.[102]

ii. Implicit Interference and the Parties' Incentives

Apart from an express contractual grant to an ALF supplier of the right to approve a settlement offer, the terms of an ALF transaction may affect the calculus of plaintiffs considering whether to settle a claim. A plaintiff may be reluctant to accept what would otherwise be a reasonable settlement offer because of a contractual obligation to repay a supplier a substantial portion of the proceeds of the settlement. For example, in the *Rancman* case, the Ohio Supreme Court was worried about the effect on settlement of the supplier's right to receive the first $16,800 of settlement proceeds, in exchange for having previously provided the plaintiff with $6,000.[103] The court noted that, assuming the plaintiff was also obligated to pay her attorney a 30% contingency fee, she would be indifferent between a settlement offer of $24,000 and nothing at all, because if she received nothing she would be permitted to keep the $6,000 advanced by the supplier.[104] Thus, the plaintiff would have an absolute disincentive to settle for anything less than $24,000. (Compounding the disincentive is the fact that the nonrecourse nature of ALF means that there is no downside for the plaintiff in going to trial, because settling for less than the amount owed to the ALF supplier yields the plaintiff nothing, while losing at trial means owing nothing to the ALF supplier, so the plaintiff still receives nothing.) On the assumption that $24,000 would otherwise be a reasonable settlement offer, the presence of ALF seems to have an adverse impact on the salutary goal of terminating litigation by settlement.[105]

Ironically, depending on the specifics of a funding agreement, ALF may also over-incentivize settlements if plaintiffs who are recipients of ALF funding are concerned about the escalating obligation to repay. While some ALF contracts tie the amount owed to the amount of the judgment or settlement, other agreements set the repayment amount with reference to the

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[100] *See generally* Grace M. Giesel, *Enforcement of Settlement Contracts: The Problem of the Attorney Agent*, 12 GEO. J. LEGAL ETHICS 543 (1999).
[101] *See* RESTATEMENT § 22 & Reporter's Note.
[102] *See* MODEL RULE 1.2(c) (only reasonable limitations on scope of representation are permissible); MODEL RULE 1.16(a)(1) (withdrawal required where representation would result in violation of the rules of professional conduct).
[103] *Rancman v. Interim Settlement Funding Corp*., 789 N.E.2d 217 (Ohio 2003).
[104] *Id.* at 220.
[105] *See also Weaver, Bennett & Bland, P.A. v. Speedy Bucks, Inc.*, 162 F. Supp. 2d 449 (W.D.N.C. 2001) (plaintiff refused settlement offer of $1,000,000 because repayment obligations to suppliers made it a losing proposition to settle for anything less than $1,200,000).

time elapsed since the funding was made.[106] A plaintiff may therefore have an incentive to accept an early but low settlement, rather than going to trial or waiting for a better settlement offer, because the plaintiff's net recovery after repaying the supplier would be higher in the early stages of litigation.

The ethical issue for lawyers is how such disincentives on the part of their clients affect their exercise of independent professional judgment. Not all situations that are unpleasant *ex post* are the result of decisions that were unreasonable *ex ante*. Assuming the client had been fully informed of all the material terms of the ALF transaction and that the client had sought legal advice before entering into the transaction, a reasonable attorney appropriately exercising independent judgment might have advised the client in the above example to accept the $6,000 in funding in exchange for an obligation to repay the first $16,800 out of settlement proceeds. If the client were short of cash and facing an emergency such as eviction or the urgent need for a medical procedure, the client's short-term need for funds may have been a more important consideration than the *ex post* disincentive to accept what would otherwise be a reasonable settlement offer. Perhaps the client's receipt of short-term funds enabled the client to persist in the litigation and receive a better settlement offer than would have been available if the client were forced to settle prematurely. Similarly, a client who agreed to an early settlement offer because it maximized the client's net recovery may have acted reasonably, given the client's presumed desire to receive payment up front in exchange for some of the value of the cause of action.

A lawyer's duty is to provide competent advice to the client considering an offer of settlement.[107] The lawyer should consider what is best for the client, all things considered. If, in the lawyer's judgment, the client would be better off rejecting a settlement offer and going to trial, then the lawyer should inform the client of this judgment, although the authority to accept or reject the settlement offer remains with the client.[108] One of the factors relevant to the client's decision might be the obligation to pay the fee charged by the ALF supplier. Other factors unrelated to the merits of the lawsuit may be present as well, such as the client's risk tolerance, discount rate, need for funds, and preferences regarding a public trial. The presence of ALF is not different in kind from the other factors that are part of virtually any decision to settle; thus, they do not present distinctive ethical issues, beyond the duty of competence and the client's authority to make settlement decisions. All fee arrangements create conflicts of interest to some extent.[109] For example, an early settlement may result in the lawyer obtaining a higher effective hourly rate, as compared with pursuing the case through trial.[110] These conflicts do not rise to the level of a material limitation, requiring disclosure and informed consent under Model Rule 1.7(a), without some financial interest of the lawyer above and beyond the pervasive interest in obtaining compensation. If the lawyer does have some kind of extraordinary interest beyond the

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[106] *See, e.g.*, the transaction described in *Fausone v. U.S. Claims, Inc.*, 915 So. 2d 626 (Fla. Dist. Ct. App. 2005); *cf.* the court's concern in *Echeverria v. Estate of Lindner*, No. 018666/2002, 2005 WL 1083704 (N.Y. Sup. Ct. Mar. 2, 2005).

[107] *See generally* 4 RONALD E. MALLEN & JEFFREY M. SMITH, LEGAL MALPRACTICE § 31:42 (2009).

[108] *See* MODEL RULE 1.2(a).

[109] *See* RESTATEMENT § 35 cmt. b.

[110] *See* HAZARD, *supra* note 77, at 798-801 (discussion of the implicit conflicts of interest created by differences in effective hourly contingency fee rates).

fee, such as a financial investment in the ALF supplier, the lawyer must also comply with the requirements of Model Rules 1.7 (conflicts created by lawyer's financial interest) and 1.8(a) (business transactions with clients).

c. Fee Sharing: Model Rule 5.4(a)

With certain enumerated exceptions, none of which are relevant here, a lawyer may not share legal fees with a nonlawyer.[111] This prohibition is intended to protect the lawyer's professional independence of judgment.[112]

A few state ethics opinions have addressed the fee-sharing rule in connection with ALF transactions.[113] These opinions state that a lawyer may not agree to give an ALF supplier a share of or a security interest in the fee the lawyer expects to receive under a contingency fee agreement with the client. Some cases, however, have reached the opposite conclusion. In *Core Funding Group v. McDonald*, No. L-05-1291, 2006 WL 832833 (Ohio Ct. App. Mar. 31, 2006), the Ohio Court of Appeals stated that it is not inappropriate for a lender to take a security interest in an attorney's accounts receivable, to the extent permitted by commercial law. This is an ordinary secured transaction and does not violate the prohibition on sharing fees with a nonlawyer, the court concluded. Following these principles, no prohibited fee splitting would be involved if the lawyer repays interest on a loan taken out by the lawyer to fund the litigation.

d. Third-party Payment of Fees: Model Rules 1.8(f) and 5.4(c)

Two provisions of the Model Rules seek to limit the influence of third-party payors of attorneys' fees. Model Rule 1.8(f) prohibits lawyers from accepting compensation from a third party for the representation of a client unless the client gives informed consent, there is no interference with the lawyer's exercise of independent professional judgment, and confidential information is protected as required by Model Rule 1.6. Model Rule 5.4(c) reinforces the protection of independent professional judgment by directing lawyers not to "permit a person who . . . pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such services." These rules overlap with, and reinforce, the lawyer's general obligation stated in Model Rule 2.1 to "exercise independent professional judgment and render candid advice." As noted previously, in connection with the decision to settle, many ALF suppliers disclaim any effort to regulate the decision-making of lawyers. Even without this disclaimer by the suppliers, however, Model Rules 1.8(f), 2.1, and 5.4(c) require lawyers to, in effect, insist that suppliers not attempt to regulate the professional judgment of lawyers. If the supplier attempts to interfere with the lawyer's professional judgment, a lawyer would have no choice but to withdraw from the representation.[114]

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[111] MODEL RULE 5.4(a).

[112] MODEL RULE 5.4, cmt. [1].

[113] *See*, *e.g.*, Ohio Supreme Court Bd. of Comm'rs on Grievances and Discipline, Advisory Op. 2004-2 (2004); Utah State Bar Ethics Advisory Opinion Comm., Advisory Op. 97-11 (1997); Va, State Bar Standing Comm. on Legal Ethics, Advisory Op. 1764 (2002).

[114] *See* MODEL RULE 1.16(a)(1) (withdrawal mandatory where representation would result in violation of the rules of professional conduct).

These Rules do not apply to purely passive investments. Model Rule 1.8(f) is not applicable to ALF transactions that do not involve the payment of "compensation for representing a client." If a tort plaintiff, for example, receives $10,000 in exchange for a promise to repay the supplier out of the proceeds of a judgment or settlement, the lawyer is not receiving compensation from the supplier. Similarly, Model Rule 5.4(c) applies only to attempts to direct the lawyer's exercise of judgment by "a person who . . . pays the lawyer." The same hypothetical supplier who obtains an assignment of a share of a tort plaintiff's claim for $10,000 is not paying the lawyer. Nevertheless, the lawyer always has a duty under Model Rule 2.1 to ensure that the lawyer is exercising independent professional judgment solely for the benefit of the client.

B. Confidentiality, Privilege, and Work Product

As part of their underwriting process, ALF suppliers often require the lawyer to release information or to provide a litigation assessment referencing such information.[115] That information is manifestly relevant to the decision of the ALF supplier. Such disclosures also clearly involve potential waivers of confidentiality and privilege that require the client's consent. A lawyer must exercise reasonable care to preserve the confidentiality of information protected by Model Rule 1.6, and to safeguard against inadvertently waiving the protection of the attorney-client privilege and the work product doctrine.[116]

In public comments, many ALF suppliers stated that they do not seek access to information covered by the attorney-client privilege.[117] On the other hand, some agreements between ALF suppliers and clients have provided for the supplier to have a right to inspect all documents, including those covered by the attorney-client privilege.[118]

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[115] *See, e.g.*, *Fausone v. U.S. Claims, Inc.*, 915 So. 2d 626, 628 (Fla. Dist. Ct. App. 2005), *aff'd*, 931 So.2d 899 (Fla. 2006) ("[tort plaintiff's] attorneys also provided [the supplier] with information about her claim to assist [the supplier] in deciding whether to advance her funds"). *See also* Emanuel, *supra* note 1, at 8 (quoting application and disclosure form provided by LawCash, a consumer ALF supplier, which informs the claimants lawyer: "We might ask you to provide medical reports, emergency room reports, accident reports, expert testimony, insurance information, information about the current status of the litigation, and any other details that would help us to make our decision."). Some of the information sought here may be covered by the attorney-client privilege (e.g. "current status of the litigation" if it revealed confidential attorney-client communications); other information might be protected by the work product doctrine (e.g. expert reports). All of it would be subject to the duty of confidentiality in Model Rule 1.6(a).

[116] *See* MODEL RULE 1.6, cmts. [16]–[17].

[117] *See, e.g.*, Comments of Juridica Capital Mgmt. Ltd. to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. 2 (Feb. 17, 2011) (on file with author) ("Our experience is that ALF funders generally do not need access to privileged or confidential information in order to make financing decisions. We perform our due diligence by relying primarily on publicly-filed pleadings and memoranda and other non-privileged materials. We do not seek attorney-client privileged information."); Comments of Oasis Legal Finance/Alliance for Responsible Consumer Legal Funding to the Am. Bar Ass'n Working Group on Alternative Litig. Fin. 4 (Apr. 5, 2011) (on file with author) ("By and large, consumer legal funding companies have no need to request privileged information from attorneys regarding their clients.").

[118] *See, e.g.*, Mich. State Bar Standing Comm. on Prof'l Ethics, Advisory Op. RI-321 (2000) (discussing an agreement between a civil tort plaintiff and an unnamed ALF supplier in which the supplier is "entitled to inspect all records, including all privileged attorney-client records, relating to the collateral") (internal quotation marks omitted).

Lawyers considering disclosure of information to ALF suppliers must be aware of three distinct but overlapping legal doctrines: The duty of confidentiality (as provided for by the Model Rules and agency law), the evidentiary attorney-client privilege, and the work-product doctrine (with its common law origin and codification in the rules of civil procedure). Questions of the scope of duty, client consent, and particularly waiver of protection vary subtly among these confidentiality-related doctrines.

1. Duty of Confidentiality: Model Rule 1.6

A lawyer must not disclose "information relating to the representation of a client" without the client's informed consent, unless the disclosure is impliedly authorized in order to carry out the representation.[119] The scope of the duty of confidentiality is significantly broader than the attorney-client privilege (see below), which protects only communications made in confidence between attorney and client, for the purpose of obtaining legal assistance.[120] The duty of confidentiality imposes duties on lawyers to safeguard information (Model Rule 1.6 cmt. [16]), but it does not create an evidentiary privilege that may be asserted in response to an official demand for information, such as a subpoena or a question at trial or in a deposition. However, competent representation does require an attorney to exercise reasonable care to ensure that the attorney-client privilege and work product protection are not inadvertently

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[119] MODEL RULE 1.6(a).

[120] There is considerable jurisdictional variation with respect to the definition of confidential information. For example, the District of Columbia and New York retain the Model Code's distinction between confidences (communications protected by the attorney-client privilege) and other information to which the duty of confidentiality is applicable. The definition of non-privileged protected information is narrower than the expansive Model Rule 1.6 term, "information relating to the representation." "Secrets" in the D.C. rules include "other information gained in the professional relationship that the client has requested be held inviolate, or the disclosure of which would be embarrassing, or would be likely to be detrimental, to the client." D.C. RULES OF PROF'L CONDUCT R. 1.6(b). New York similarly defines protected confidential information as follows:

> "Confidential information" consists of information gained during or relating to the representation of a client, whatever its source, that is (a) protected by the attorney-client privilege, (b) likely to be embarrassing or detrimental to the client if disclosed, or (c) information that the client has requested be kept confidential. "Confidential information" does not ordinarily include (i) a lawyer's legal knowledge or legal research or (ii) information that is generally known in the local community or in the trade, field or profession to which the information relates.

N.Y, RULES OF PROF'L CONDUCT R. 1.6(a). Finally, California Business and Professions Code § 6068(e) (incorporated by reference into proposed California Rule 1.6(a)) requires lawyers to protect the confidences and secrets of clients. The scope of protected information has been defined as "information gained by virtue of the representation of a client, whatever its source, that (a) is protected by the lawyer-client privilege, (b) is likely to be embarrassing or detrimental to the client if disclosed, or (c) the client has requested be kept confidential." *See* proposed CAL. RULES OF PROF'L CONDUCT R. 1.6 cmt. [3].

Some disclosures of information relating to representation, which would be prohibited under Model Rule 1.6(a), would not violate the duty of confidentiality in jurisdictions such as New York, D.C., or California, which preserve the Model Code's narrower definition of protected information.

waived.[121] Thus, lawyers representing clients in connection with ALF transactions must exercise reasonable care to ensure that confidential client information is protected.

A client may give informed consent to the disclosure of confidential information.[122] As noted in connection with conflicts of interest, informed consent means the client's agreement "after the lawyer has communicated adequate information and explanation about the material risks and reasonably available alternatives to the proposed course of conduct."[123] One of the risks of disclosing confidential information to an ALF supplier is that the disclosure will cause a waiver of the attorney-client privilege or (less likely) the protection of the work product doctrine. The following section discusses the law governing the assertion and waiver of the attorney-client privilege. Because there is considerable uncertainty with respect to some aspects of this law, such as the applicability of the common-interest exception to the principle that voluntary disclosure waives the privilege, a client's informed consent to share confidential information with an ALF supplier must be predicated upon full disclosure of the risk of a loss of privilege.

In Case 2, the client has come to the lawyer subject to a pre-existing contractual obligation to share all relevant information with an ALF supplier and to waive any applicable duty of confidentiality. The client may or may not appreciate the significance of these contract terms. Thus, an attorney should explain the risks associated with sharing confidential information with the ALF supplier and should obtain the client's informed consent to the attorney providing this information to the supplier.

2. Attorney-Client Privilege

The attorney-client privilege is an evidentiary doctrine with deep roots in the common law. It protects confidential communications from discovery by opposing parties in litigation. Because it is a matter for case-by-case development, there is considerable variation in the specific contours of the privilege, both in terms of prerequisites for coverage and waiver doctrines. This Informational Report will discuss privilege and waiver in general terms, but attorneys must be mindful of differences among jurisdictions, and also of the fact-specific nature of many privilege and waiver cases. It is also important to emphasize that the attorney-client privilege is an aspect of state and federal evidence law, and develops independently of the duty of confidentiality recognized in state and federal rules of professional conduct.

a. Scope

The attorney-client privilege covers communications made between privileged persons, in confidence, for the purpose of obtaining or providing legal assistance for the client.[124] "Privileged persons" include the attorney, the client, and agents of the lawyer who facilitate the

[121] *Cf.* RESTATEMENT § 79 cmt. h (no waiver if the client or lawyer took reasonable precautions to safeguard against inadvertent disclosure).
[122] MODEL RULE 1.6(a).
[123] MODEL RULE 1.0(e).
[124] RESTATEMENT § 68.

representation.[125] Experts retained by the lawyer to facilitate the representation, such as accountants and economists, may be considered privileged persons if they facilitate the client-lawyer communication – in effect acting as translators of technical material.[126]

The definition of privileged persons is related to the issues considered below, regarding the common interest doctrine, which functions as an exception to the rule of waiver by voluntary disclosure. For example, the disclosure by an attorney of privileged communications to a liability insurer, pursuant to a cooperation clause in an insurance policy, may not waive the privilege with respect to third parties. The conclusion of non-waiver may be based upon the premise that the insurer is also a privileged person, along with the attorney and client.[127] Alternatively, it may be based upon the premise that the client and the insurer are either jointly represented clients[128] or have a common interest[129] in the litigated matter.[130]

b. Waiver by Voluntary Disclosure

Disclosure of privileged communications to anyone other than another privileged person waives the privilege and the communication is subject to discovery.[131] Because the privilege protects *confidential* communications between attorney and client, conduct by either party that is inconsistent with the ongoing confidentiality of the communication destroys the rationale for the privilege. Courts generally take a strict approach to privilege waivers, finding that any voluntary disclosure of private communications will waive the privilege. Some courts have recognized a doctrine of "limited waiver," permitting disclosure to some parties (generally government agencies) without waiving the privilege with respect to other parties (such as private litigants).[132] The considerable majority of courts, however, do not recognize limited waiver; thus, any disclosure of confidential communications will waive the privilege that otherwise would have

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[125] RESTATEMENT § 70.
[126] *See, e.g., U.S. v. Kovel*, 296 F.2d 918 (2d Cir. 1961).
[127] *See* RESTATEMENT § 70 cmt. f & Reporter's Note.
[128] *See* RESTATEMENT § 75.
[129] *See* RESTATEMENT § 76.
[130] *See* PAUL R. RICE, ATTORNEY-CLIENT PRIVILEGE IN THE UNITED STATES § 9:64 (2d ed. & Supp. 2010).
[131] *See generally id.* § 9:28.
[132] *See, e.g., Diversified Indus. v. Meredith*, 572 F.2d 596 (8th Cir. 1978). As is often the case with respect to the attorney-client privilege, courts use terminology inconsistently. *In re Columbia/HCA Healthcare Corp. Billing Practices Litig.*, 293 F.3d 289 (6th Cir. 2002) uses the term "selective waiver" to refer to the attempt by a party to share confidential communications with the government but continue to assert the privilege to thwart discovery of the communications by a private litigant. A leading treatise on the attorney-client privilege, however, uses the term "selective waiver" to refer to disclosure of one part of a privilege communication, while seeking to assert the privilege as to the remainder of the communication. *See* RICE, *supra* note 130, § 9:80. This kind of partial subsequent disclosure is related to the idea of "subject matter" waivers – i.e. that the partial disclosure of a communication waives the privilege with respect to all communications on the same subject matter. *See* RESTATEMENT § 79 cmt. f. This Informational Report adopts the term "limited waiver," *see* RICE, *supra* note 130, § 9:88, to refer to what the *Columbia/HCA* court calls "selective waiver," which is the context in which waiver issues would arise in connection with ALF transactions.

protected the communications from discovery.[133] This is the case even if the selective or limited disclosure is made subject to a confidentiality agreement.

Thus, under privilege law in most jurisdictions, sharing of privileged communications with an ALF supplier is a voluntary disclosure that may effect a waiver of the attorney-client privilege. A court reaching the contrary conclusion of non-waiver may reason that the supplier is another privileged party, along with the attorney and client, or that the supplier and the client have a common interest in the litigated matter.

c. Common Interest Exception

The common interest exception is not, strictly speaking, an expansion of the attorney-client privilege. Rather it is a rule of non-waiver that stands as an exception to the general principle that disclosure of privileged communications to a non-privileged party waives the privilege.[134] The common interest exception is closely related to the privilege for jointly represented co-parties,[135] with the difference being that parties may have a common interest even if they are not represented by the same lawyer. Courts and lawyers sometimes use the term "joint defense" privilege to refer to these situations, but the common interest doctrine is not limited to defendants, to formal parties to litigation, or to litigated matters.[136] The most important predicate for the application of this doctrine is that the multiple parties have a common interest in the matter and agree to share confidential information concerning the matter.

There is a significant unresolved question of whether disclosure of privileged communications to an ALF supplier waives the privilege – that is, whether the ALF supplier and the client have interests sufficiently in common to fall within the rule of non-waiver. One case has held that materials protected under the attorney-client privilege provided to an ALF firm *do not* fall within the common interest exception.[137] The court stressed that, for the common-interest doctrine to apply, there must be a commonality of legal, not merely business interests.[138] It suggested that the test to be applied is whether the disclosures would not have been made, but for the sake of securing or providing legal representation.[139] Because the party seeking discovery failed to satisfy this burden, the district court concluded that the magistrate judge's order to produce the documents claimed to be privileged was not clearly erroneous.

Another case is sometimes cited for the proposition that materials may be provided to investors without waiver, because the disclosure falls within the common-interest exception.[140]

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[133] *See, e.g.*, *In re Columbia/HCA Healthcare Corp. Billing Practices Litig.*, 293 F.3d 289 (6th Cir. 2002) (citing cases, and finding waiver as to all parties resulting from disclosure of documents by privilege-holder to the Department of Justice).
[134] *See* RESTATEMENT § 76(1).
[135] *See* RESTATEMENT § 75.
[136] *See* RESTATEMENT § 76 cmt. b & Reporter's Note.
[137] *Leader Techs. v. Facebook, Inc.*, 719 F. Supp. 2d 373 (D. Del. 2010).
[138] *Id.* at 376.
[139] *Id.*
[140] *Mondis Tech. v. LG Electronics*, Nos. 2:07–CV–565–TJW–CE, 2:08–CV–478–TJW, 2011 WL 1714304 (E.D. Tex. May 4, 2011).

It is important to note, however, that this case involved disclosure of documents protected by the work product doctrine. As discussed below, the work product doctrine is subject to a different waiver standard, as compared with the attorney-client privilege. The privilege may be lost through the public disclosure of confidential communications. Protection of the work product doctrine, by contrast, is lost only where the disclosure increases the likelihood that the adversary will come into possession of the documents. The district court in *Mondis Tech. v. LG Electronics* concluded that the disclosure to prospective investors of documents reflecting the plaintiff's litigation strategy and licensing plan "did not substantially increase the likelihood that the adversary would come into possession of the materials."[141] This reasoning does not invoke the idea of a commonality of interests between the plaintiff and the investors, and therefore this case should not be relied upon in support of a conclusion of non-waiver of the attorney-client privilege.

3. Work Product Doctrine

The work product doctrine has common law origins,[142] but it has been codified in the Federal Rules of Civil Procedure and most state rules of procedure.[143] The purpose of the work product doctrine is to protect the thoughts, mental impressions, and strategies of lawyers from being discovered by opposing parties in litigation. As Justice Jackson put it in his concurring opinion in the *Hickman* case, "discovery was hardly intended to enable a learned profession to perform its functions on wits borrowed from the adversary."[144] This well-known quote also shows that the work product doctrine is justified with reference to the functioning of the adversary system of litigation, not privacy concerns generally. Thus, work product protection is narrower in scope than either the attorney-client privilege or the duty of confidentiality. It extends to:

> documents and tangible things otherwise discoverable . . . prepared in anticipation of litigation or for trial by or for another party or by or for that other party's representative (including the other party's attorney, consultant, surety, indemnitor, insurer, or agent)...[145]

"Ordinary" work product, which is to say material other than an attorney's mental impressions, theories, and opinions, may be discovered upon a showing of substantial need and an inability by the party to obtain the equivalent by other means. "Opinion" work product, on the other hand, is hardly ever discoverable.

Because work product protection focuses on the privacy of the lawyer's strategies and mental impressions, and is also tightly linked with the process of litigation, the analysis of waiver of work product protection differs somewhat from the rules governing waiver of the attorney-client privilege. Generally only disclosures that substantially increase the likelihood of

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[141] *Id.* at *3.
[142] *See Hickman v. Taylor*, 329 U.S. 495 (1947).
[143] *See, e.g.*, FED. R. CIV. P. 26(b)(3).
[144] *Hickman v. Taylor*, 329 U.S. at 516 (Jackson, J., concurring) (internal alterations omitted).
[145] FED. R. CIV. P. 26(b)(3).

documents falling into the hands of an adversary in litigation are deemed to waive the protection of the work product doctrine.[146] As discussed above, in connection with the common-interest rule of non-waiver of the attorney-client privilege, the district court in *Mondis Tech. v. LG Electronics* concluded that a party could share documents prepared by a lawyer, containing information about legal strategy, with investors without waiving the work product protection that applied to the documents. The reason for not finding waiver in this case was that the presentation to investors did not substantially increase the likelihood that the documents would come into possession of the plaintiff's adversary in litigation.

4. Third-Party Evaluations

Lawyers are frequently requested to provide opinion letters to various third parties, attesting to their clients' compliance with legal requirements. For example, lenders often seek assurances that they will have a valid security interest in property the client is using as collateral for a loan.[147] Lawyers are permitted to provide an evaluation to a third party of a matter affecting the lawyer's client, as long as doing so is compatible with other aspects of the client-lawyer relationship.[148] If there is a significant risk that the client's interests will be affected materially and adversely by providing the evaluation, the lawyer must first obtain the client's informed consent.[149] If there is no significant risk to the client, the lawyer is impliedly authorized (by the client's direction to provide the third-party evaluation) to disclose information that would otherwise be protected by the duty of confidentiality.[150]

An ALF supplier may seek information about a client's case as part of the funding process.[151] As discussed below, there may be a significant risk that any information disclosed to an ALF supplier will no longer be covered by the attorney-client privilege. Thus, the client's informed consent is required before disclosure is permitted. In order to obtain informed consent, the lawyer must explain the risk of waiver of the privilege, advise the client whether the benefits of disclosure outweigh this risk, and advise the client of reasonably available alternatives.[152]

C. Fees

1. Reasonableness: Model Rule 1.5(a)

A lawyer may not charge an unreasonable fee, or an unreasonable amount for expenses arising out of the representation.[153] The reasonableness of fees and expenses is evaluated using

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[146] *See* 8 CHARLES A. WRIGHT, ET AL., FEDERAL PRACTICE AND PROCEDURE § 2024.
[147] *See, e.g.*, *Greycas, Inc. v. Proud*, 826 F.2d 1560 (7th Cir. 1987) (legal malpractice case).
[148] MODEL RULE 2.3(a).
[149] MODEL RULE 2.3(b).
[150] MODEL RULE 2.3 cmt. [5].
[151] *See, e.g.*, Emanuel, *supra* note 1, at 8 (quoting application and disclosure form provided by LawCash, a consumer ALF supplier, which informs the claimants lawyer that "[w]e might ask you to provide . . . information about the current status of the litigation, and any other details that would help us to make our decision").
[152] *See* MODEL RULE 1.0(e).
[153] MODEL RULE 1.5(a). The ABA Committee on Ethics and Professional Responsibility has concluded that the reasonableness standard applies to both fees and expenses. *See* ABA Comm. on Ethics and Prof'l Responsibility,

an eight-factor test,[154] but judicial decisions tend to focus on two factors: (1) Did the client make a free and informed decision to enter into the contract with the lawyer, and (2) does the contract provide for a fee within the range commonly charged by other lawyers in similar circumstances?[155] Any fees for representing a client, including contingency fees and, as discussed below, financing charges passed through by the lawyer to the client as a result of the lawyer obtaining funding for the representation, must satisfy the reasonableness standard of Rule 1.5(a). Concern has also occasionally been expressed that lawyers' involvement as principals in ALF transactions may be a way of covertly increasing the lawyers' contingency fees.[156] There are many other restrictions on lawyers participating personally in ALF transactions, including the prohibitions in Model Rule 1.8 on providing financial assistance to a client and on acquiring a proprietary interest in the client's cause of action. If the structure of a funding transaction were in compliance with these rules, however, a lawyer's total compensation for providing legal services would still need to meet the reasonableness requirement of Rule 1.5(a).

2. Passing Borrowing Costs to Clients

Law firms representing clients on a contingency fee basis typically advance the cost of professional services provided to firm lawyers and support staff, as well as out-of-pocket expenses such as filing fees, expert witnesses, and court reporters. In some cases, the projected cost of a protracted lawsuit exceeds the firm's ability to finance these expenditures out of its ordinary operating budget. In these circumstances, firms have sought loans or lines of credit from commercial lenders. In some cases lawyers have also sought to pass along the interest charges to the client as an expense, as opposed to absorbing these borrowing costs as part of the firm's overhead that would be reflected in the fee for services portion of the recovery owed to the firm.

It is generally permissible to pass along the cost of disbursements made by lawyers on behalf of clients in connection with representation in a matter. "[T]he actual amount of disbursements to persons outside the office for hired consultants, printers' bills, out-of-town travel, long-distance telephone charges, and the like ordinarily are charges in addition to the lawyer's fee."[157] However, it is improper for a lawyer to add a surcharge to these disbursements, or to charge the client for general overhead expenses. Numerous state ethics opinions have considered this question and concluded that it is permissible to pass on to the client interest charges on funds borrowed in order to finance the costs and expenses of litigation, provided the lawyer fully discloses the terms of the loan and the interest rate is reasonable.[158] The Kentucky

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Formal Op. 93-379 (1993), at 7 ("we believe that the reasonableness standard explicitly applicable to fees under Rule 1.5(a) should be applicable to [disbursements and expenses] as well").

[154] *See* MODEL RULE 1.5(a)(1)-(8),

[155] *See* RESTATEMENT § 34 cmt. c.

[156] *See, e.g., Fausone v. U.S. Claims, Inc.*, 915 So.2d 626, 630 (Fla. Dist. Ct. App. 2005).

[157] *See* RESTATEMENT § 38 cmt. e.

[158] *See* Ariz. State Bar Comm. on the Rules of Prof'l Conduct, Formal Op. 01-07 (2001); Ky. Bar Ass'n Ethics Comm., Formal Op. E-420 (2002); Me. Bd. Of Overseers of the Bar Prof'l Ethics Comm'n, Formal Op. 177 (2001); Mich. State Bar Standing Comm. on Prof'l Ethics, Advisory Op. RI-336 (2005); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 754 (2002); N.Y. State Bar Ass'n Comm. on Prof'l Ethics, Advisory Op. 729 (2000); N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 1997-1 (1997); N.C. State Bar Ethics Comm.,

opinion adds the requirement that the transaction be treated as a business transaction between the lawyer and client, subject to all of the requirements of Rule 1.8(a). Although not citing Rule 1.8(a), the Maine opinion imposes similar requirements – full disclosure of the terms of the transaction and the informed consent of the client, and fairness to the client of the substantive terms of the transaction. In no event may the lawyer surcharge the client by charging more than the amount of interest actually paid to the lender.

In Case 4, the lawyer incurred substantial borrowing costs to finance the litigation on behalf of the plaintiffs. Ethics opinions in several states indicate that the lawyer may permissibly charge these costs to the plaintiffs, assuming two requirements are satisfied. First, the total fee must be reasonable, under the standards of Rule 1.5(a). Second, because the lawyer represented the plaintiffs on a contingent fee basis, the lawyer was required to clearly disclose, in a writing signed by the client, whether the client would be liable for interest expenses, whether these expenses would be deducted from the recovery, and whether this deduction would occur before or after the lawyer's fee was calculated.[159] The hypothetical states that the lawyer did not clearly disclose in the retainer agreement that the lawyer may incur interest expenses and subsequently pass them along to the client. Thus, the lawyer may lose the entitlement to charge these expenses to the client, due to non-compliance with the disclosure requirements of Rule 1.5(c). If clear, understandable written disclosure had been made, however, there is no reason in principle why these expenses could not be charged to the clients. Fact issues may of course arise concerning the adequacy of the disclosure.

D. Competence and Communication: Advising in Connection with ALF Transactions

A lawyer must communicate with a client regarding matters material to the representation.[160] A client who wishes to enter into a funding transaction with an ALF supplier incurs financial risks that must be adequately explained by a lawyer representing the client in connection with that transaction.

A party to litigation, whether a plaintiff or defendant, may have entered into or considered entering into an ALF transaction without the knowledge of that party's lawyer. The lawyer may subsequently be called upon to advise the client about the implications of the transaction or contemplated transaction. Case 1 presents an example of a client asking the lawyer for advice concerning whether to sell a portion of his personal-injury claim to an ALF supplier. Lawyers must provide competent representation, using the "legal knowledge, skill, thoroughness and preparation reasonably necessary to the representation."[161] If the lawyer is unfamiliar with transactions of this nature, he or she must either acquire the appropriate knowledge through reasonable study and preparation,[162] associate with an experienced lawyer, or

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Formal Op. 2006-12 (2006); Pa. Bar Ass'n Comm. on Legal Ethics and Prof'l Responsibility, Formal Op. 2003-18 (2003); Utah State Bar Ethics Advisory Opinion Comm., Advisory Op. 02-01 (2002).

[159] *See* MODEL RULE 1.5(c).

[160] MODEL RULE 1.4.

[161] MODEL RULE 1.1.

[162] Although a lawyer may be able to satisfy the duty of competence through study and preparation, it may not be reasonable to bill the client for the time spent acquiring this new expertise. *See* MODEL RULE 1.5(a); *see also In re*

refer the client to another lawyer with established competence.[163] The variation on Case 1 is intended not only to show that a lawyer may have acquired the relevant expertise through experience with similar transactions, but also the kinds of issues a lawyer should be aware of when advising a client. The extent of control sought by the supplier, whether the supplier seeks access to confidential information, and the material terms of the financing transaction are all relevant to the advice the lawyer should give the client.

Case 2 illustrates some of the risks that unsophisticated users of ALF products face. One problem for the lawyer representing this plaintiff, however, is that the agreement was entered into without legal counsel, prior to the plaintiff's retention of the lawyer. If a reasonable lawyer would conclude that the terms of the financing are substantively unfair and unreasonable from the plaintiff's point of view, the lawyer may advise the client to attempt to renegotiate the transaction. On the other hand, a reasonable lawyer may conclude that the transaction was not unfair from the plaintiff's point of view, given the difficulty the plaintiff would otherwise have in obtaining funds and the riskiness of this investment, from the point of view of the ALF supplier.

In both Case 1 and Case 2, competent advising requires, at a minimum, that a lawyer be aware of potential risks to the client associated with ALF transactions, such as the possibility of waiver of the attorney-client privilege. Other risks may be present depending on the terms of the transaction. For example, a client who sells a portion of a cause of action in exchange for periodic investments by an ALF supplier may be exposed to the risk of the subsequent insolvency of the supplier.

V. Conclusion

The market for alternative litigation finance involves suppliers and customers who demand this form of financing. Because of this demand, and because of the complexity of regulation in various jurisdictions, the specific form of ALF transactions will undoubtedly continue to evolve. The Commission on Ethics 20/20 has accordingly set out to define general principles of professional responsibility that are applicable to lawyers representing clients who are involved in ALF funding. Lawyers must adhere to principles of professional independence, candor, competence, undivided loyalty, and confidentiality when representing clients in connection with ALF transactions. In the event that the lawyer's involvement in the funding process significantly limits the lawyer's capacity to carry out these professional obligations, the lawyer must fully disclose the nature of this limitation, explain the risks and benefits of the proposed course of action, and obtain the client's informed consent.

Respectfully Submitted,

ABA Commission on Ethics 20/20

Fordham, 668 N.E.2d 816 (Mass. 1996) (attorney's fee charged by a civil litigator unreasonable where, *inter alia*, he spent considerable time learning criminal law and procedure in order to provide competent representation to a client in a driving-under-the-influence case).

[163] *See* MODEL RULE 1.1 cmts. [1], [2], [4].

February 2012

THE STATE BAR OF CALIFORNIA
STANDING COMMITTEE ON
PROFESSIONAL RESPONSIBILITY AND CONDUCT
FORMAL OPINION NO. 2020-204

ISSUE: What ethical obligations arise when a lawyer represents a client whose case is being funded by a third-party litigation funder?

DIGEST: Two types of third-party litigation funding have emerged over the last several years: consumer litigation funding, which provides funds to a plaintiff with personal injury claims, typically for personal use rather than to fund their case, and commercial litigation funding, which typically involves advancing funds to pay a plaintiff's litigation expenses or otherwise. Both types of funding are non-recourse.[1/] This opinion addresses the ethical issues that arise from such funding arrangements. The principal ethical issues are maintaining independent professional judgment and complying with the lawyer's duty of confidentiality. In commercial litigation funding arrangements, the funding agreement will likely be negotiated. If the client asks the lawyer to represent him or her in such negotiations, the lawyer should consider whether the lawyer has the experience or learning required as well as whether the lawyer has any personal interest that creates a conflict. If so, the lawyer must address those by a written disclosure that describes the relevant circumstances and material risks and then obtain the client's written consent. If the funder seeks client confidential information, the lawyer must advise the client of the risks of disclosure and obtain the client's informed consent to disclose confidential information to the funder. The lawyer should also take appropriate steps to limit the risks to the client that the disclosure of such information will effect a waiver of attorney-client privilege or work product protection which may include having the funder sign a non-disclosure agreement, appropriate labeling of shared materials as confidential or taking other steps to maintain the confidentiality of the shared materials.

[1/] Within commercial litigation funding, there are also arrangements where the lawyer or law firm is funded rather than the client, often in the form of portfolio funding for a group of cases.

AUTHORITIES INTERPRETED: Rules 1.1, 1.4, 1.6, 1.7(b), and 1.8.6 of the Rules of Professional Conduct of the State Bar of California.[2/]

STATEMENT OF FACTS

Scenario 1: Lawyer represents Client with personal injury claim who is in need of money for living expenses. Lawyer advises Client that Client may qualify for litigation funding and provides Client with a list of funders that Lawyer's clients have used. At Client's request, Lawyer reviews the agreement and explains its terms carefully, emphasizing that the interest rate on the loan is high, there is also a large administrative fee, and Client might be able to get a bank loan at a lower rate. Despite this advice, Client enters into the funding agreement.

Scenario 2: Client, a company asserting a patent claim, is interested in litigation funding to avoid tying up its cash in legal fees. Lawyer has extensive experience with third-party funding and recommends a funder with which the firm has worked previously. Prior to agreeing to fund the case, Funder asks for a memo assessing the strengths of Client's case. Lawyer tells Funder that Lawyer will seek Client's consent to share this information. Lawyer advises Client there is some risk that sharing the memo could waive applicable privileges, that the risk is lessened if the information is communicated under a non-disclosure agreement ("NDA"), and that Client must also consider that Funder will probably not fund the case without receiving Lawyer's assessment of the strength of the claims. Client authorizes Lawyer to share the memo. Because of prior good experience with Lawyer, Funder agrees to fund Client's case (the Client, in turn, is responsible for paying Lawyer's legal fees). Lawyer is able to negotiate a better than standard deal for Client because of Lawyer's relationship with Funder. Under the terms of the deal, Funder funds a portion of Lawyer's fees (the Lawyer is on a partial contingency) and pays litigation expenses. Such funds are provided to Client, who in turn pays Lawyer. Funder has the right to cease funding if it disagrees with the direction of the litigation. The funding agreement also gives Funder the right to review and approve any change in counsel, which approval will not be unreasonably withheld. Over the course of the litigation, Funder's employees communicate regularly with Lawyer.

Scenario 3: Same facts as Scenario 2, except under the funding agreement, Funder pays Lawyer's legal fees directly for the representation of Client.

[2/] Unless otherwise indicated, all references to rules in this opinion will be to the Rules of Professional Conduct of the State Bar of California in effect as of November 1, 2018.

INTRODUCTION: LITIGATION FUNDING AND ITS ANTECEDANTS

Litigation funding is the practice where a third-party unrelated to the lawsuit provides funds for litigation in return for a portion of any financial recovery. In this opinion, we consider the ethical issues an attorney may face in representing a client where litigation funding is involved.

The type of third-party litigation funding addressed by this opinion is a relatively recent development in the United States, although more common and accepted elsewhere.[3/] The ethics and social utility of this type of litigation funding are the subject of debate. Some have raised concerns that litigation funding will lead to frivolous lawsuits or that vulnerable clients may be forced to accept unfair deals.[4/] Others argue litigation funding in the United States promotes access to justice and/or diversifies thinking about litigation.[5/]

The purpose of this opinion is not to enter the normative debate about litigation funding but rather to provide guidance to attorneys as to the ethical issues that arise when dealing with a case that involves third-party funding.

DISCUSSION

A. Legality

In some states, agreements between a litigant and a stranger to the litigation by which the stranger pursues or assists in pursuing the litigant's claim and in return receives part of any recovery are prohibited under laws against champerty and maintenance. These are legal doctrines dating from the Medieval England that developed to prevent feudal lords from financing other individuals' legal claims against the financer's political or personal enemies.

Courts in states with laws against champerty and maintenance have considered whether litigation funding arrangements violate those laws. See *Charge Injection Technologies, Inc. v. E.I. DuPont De Nemours & Company* (2016) 2016 WL 937400 (finding that litigation funding contract did not violate Delaware's common law prohibition on champerty and maintenance because the funder did not exercise control over litigation); *Maslowski v. Prospect Funding Partners LLC* (2017) 890 N.W.2d 756 (finding that litigation funding agreement was unenforceable by Minnesota law against champerty).

3/ Barker, *Third-Party Litigation Funding in Australia and Europe* (2012) 8 J.L. Econ. & Pol'y 451.

4/ See, e.g., Langford, *Betting on the Client*: *Alternative Litigation Funding Is An Ethically Risky Proposition for Attorneys and Clients* (2015) 49 U.S.F. L.Rev. 237.

5/ See, e.g., Steinitz, *Whose Claim Is This Anyway? Third Party Litigation Funding* (2011) 95 Minn. L.Rev. 1268 (hereafter *Whose Claim*); DeStefano, *Nonlawyers Influencing Lawyers: Too Many Cooks in the Kitchen or Stone Soup* (2012) 80 Fordham L.Rev. 2791.

California has never recognized prohibitions against champerty or its variants. See *In re Cohen's Estate* (1944) 66 Cal.App.2d 450 [152 P.2d 485]. Such laws should not be a barrier to a litigation funder enforcing a litigation funding contract in California.[6/]

B. Duty of Competence and Duty to Communicate

A lawyer has a duty to provide competent representation, which includes applying the learning and skill reasonably necessary to perform legal services. Rule 1.1(b). A lawyer also has a duty to communicate with the client about the means by which to accomplish the client's objectives in the representation. Rule 1.4(a). To the extent the client's ability to accomplish its objectives depends on the client's ability to fund the litigation or fund the client's personal expenses while proceeding with the litigation, the lawyer's representation of the client may involve advising the client as to whether litigation funding would assist in accomplishing the client's goals. Such advice would likely need to include a discussion of the pros and cons of obtaining litigation funding and alternatives, if any.

Furthermore, a lawyer representing a client in a matter funded by a litigation funder has an obligation to understand how the funding agreement impacts the litigation. If the client asks the lawyer to advise on or negotiate a litigation funding contract, the lawyer must either have the expertise to do so, obtain such experience, or decline to provide the requested advice regarding litigation funding. See rule 1.1(c). But regardless of whether the attorney is advising a client on the funding contract, the lawyer must understand how the terms of the funding agreement impact decisions in the litigation.

C. Candid Advice and Independent Professional Judgment

Rule 2.1 provides that "[i]n representing a client, a lawyer shall exercise independent professional judgment and render candid advice." This rule dovetails with a lawyer's duty of loyalty to a client, which generally prohibits a lawyer from allowing obligations owed or potentially owed to a third-party to compromise the quality and soundness of advice offered to a client. See, e.g., *Pollack v. Lytle* (1981) 120 Cal.App.3d 931, 946 [175 Cal. Rptr. 81] (explaining how the duty of loyalty to clients should not be diluted by obligations owed to third parties, as that would be inconsistent with an attorney's duty to exercise independent professional judgment for the client). The lawyer must reasonably believe that the lawyer's independent professional judgment will not be undermined, and that the lawyer can thus provide candid advice to the client regarding the subject matter of the representation.

Rule 1.7 prohibits a lawyer from representing a client if there is a significant risk that the representation will be materially limited by the lawyer's relationships with a third person or the

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6/ See also, Los Angeles County Bar Assn. Formal Opinion No. 500 (1999) [explaining that doctrines of champerty and maintenance have not been recognized by California courts, and the concerns raised by those doctrines are addressed by other protections including sanctions for frivolous lawsuits and malicious prosecution actions].

lawyer's own interest without the lawyer's informed written consent. Rule 1.7(b). The lawyer must also reasonably believe that the lawyer can provide competent and diligent representation notwithstanding the potential conflict or relationship with a third person. Rule 1.7(d).

Rule 1.8.6 prohibits a lawyer from entering into an agreement for or accepting compensation for representing a client from one other than the client unless the client gives informed written consent, the lawyer complies with the lawyer's duty of confidentiality, and the payment arrangement will not interfere with the lawyer's independent professional judgment or with the lawyer-client relationship. The rule would apply in an arrangement where the funder pays the lawyer directly. The rule reflects the recognition that the source of the lawyer's payment is likely to have influence over the lawyer. Litigation funding, like a third-party payor, introduces a third-party with its own interests into the lawyer-client relationship, posing risks to the lawyer's independent professional judgment and the relationship of confidence between the lawyer and client. The duty of loyalty and independent professional judgment require the lawyer to act in the client's interest at all times and particularly where the client's interest might depart from the funder's.

The lawyer's independent professional judgment may also be impaired if the funding arrangement imposes limitations on the how the case is litigated. Some ethics committees have suggested that there could be circumstances in which a funding agreement imposes such limitations on the attorney's judgment that the lawyer might not be able to competently represent the client. ABA Commission on Ethics 20/20, Informational Report to the House of Delegates 23 (2012); Ohio Sup. Ct. Ethics Opn. No. 2012-3 (lawyer must ensure the alternative litigation funding company providing nonrecourse loan to client "does not attempt to dictate the lawyer's representation of the client"). Others have suggested that such arrangements are permissible with client consent. Assn. of the Bar of the City of N.Y. Com. on Prof. and Jud. Ethics, Formal Opn. No. 2011-02 (client may "agree to permit a financing company to direct strategy or other aspects of a lawsuit" and the lawyer is not prohibited from acceding to the funder's direction as long as the client consents); cf. ABA Formal Opn. No. 01-421 (lawyer hired by insurer to represent insureds may not comply with insurer's guidelines or directives relating to representation if these would "impair materially the lawyer's independent professional judgment").

The Committee does not reach a general conclusion that any particular degree of control is per se unethical. However, it is clear that where the funder has some degree of control of the litigation, the lawyer has an obligation to advise the client about the impact of such limitations on the lawyer's representation. Rule 1.4; see also ABA Formal Opn. No. 01-421 (where lawyer represents insured and the insurer imposes limitations on the representation, lawyer must communicate limitations to the client early in the representation).

A lawyer's duties are not dictated by the funding contract but by the lawyer's ethical duties. ABA Formal Opn. No. 96-403 illustrates this principle in the context of an insurance agreement. The opinion considers the ethical obligations of an attorney retained by an insurer to represent

the insured pursuant to a contract that gave the insured control over settlement within policy limits where the client objects to the proposed settlement. The ABA opined that the lawyer could not settle against his client's wishes. Instead, the lawyer was obligated to discuss with the client, the client's legal rights, explain the consequences of rejecting the settlement and let the client decide.

This opinion stands for the proposition that a litigation funding agreement may be a fact that impacts the advice the lawyer gives a client, but it does not alter the lawyer's ethical obligation to pursue the client's best interest. *Id.* ("Whatever the rights and duties of the insurer and insured under the insurance contract, that contract does not define the ethical responsibilities of the lawyer to his client.") See also, Md. State Bar Ass'n, Comm. on Ethics Opn. No. 00-45 (opining that where the client wishes to terminate a lawyer, the lawyer must abide by the client's wishes regardless of whether the client's terminating the lawyer is a breach of the funding agreement).

D. Protecting Confidential Information

In order to determine whether to invest in a case, funders will likely require information about the case at the outset. A prospective funder may ask for the attorney's analysis of the merits of the case or other privileged materials. Once a funder has agreed to fund the case, that agreement will likely be memorialized in a contract which may reflect how the funder values the case which is likely to be based on the attorney's analysis. As the case proceeds, there may continue to be communications between the funder and client or between the funder and the client's counsel.

Rule 1.6 prohibits a lawyer from sharing confidential information without the client's informed consent. In order for the client's consent to be informed, the lawyer must inform the client about "the relevant circumstances and the material risks, including any actual and reasonably foreseeable adverse consequences." Such risks include the client's adversary may seek to compel communications between the funder and the client or lawyer and a court may hold that the sharing effected a waiver of otherwise available evidentiary privileges.

E. Application to Hypothetical Scenarios

Scenario 1

In Scenario 1, Client with a personal injury claim entered into a funding agreement to pay his living expenses while his lawsuit is ongoing. Lawyer recommended that Client explore litigation funding, but also after reviewing the terms of the funding agreement, advises Client accurately about the downsides of the funding including that Client might be able to get a bank loan at a lower rate. Did Lawyer meet his ethical duties in each of these steps?

First, there is nothing unethical about a lawyer recommending a client consider litigation funding as long as there is no legal bar to the client entering into such a transaction. This Committee has previously opined that a lawyer may refer a client to a real estate broker to

obtain a loan to be used for legal fees. Cal. State Bar Formal Opn. No. 2002-159. Similarly, a lawyer may ethically provide information and introductions to a litigation funder.

In Scenario 1, the Client asked the Lawyer to review the terms of the funding agreement and the Lawyer gave Client an independent and objective assessment. The fact pattern is silent on the Lawyer's experience reviewing litigation funding agreements. The Lawyer must consider whether Lawyer has the skills necessary to advise the client and, if not, either tell Client it is outside the Lawyer's expertise, obtain the necessary understanding of litigation financing in order to adequately advise Client regarding the agreement proposed, or consult with another lawyer he reasonably believe has the requisite expertise. Rule 1.1.

Scenario 2

In Scenario 2, Lawyer advises Client on choice of funder and negotiates the funding contract on behalf of Client. Does Lawyer have a conflict in providing these services? The facts state that the Lawyer has a preexisting relationship with Funder, that Funder will be partially paying the law firm's fees and that certain terms of the funding agreement are advantageous to the law firm.

Under rule 1.7, if any of those circumstances or their combination creates a significant risk that Lawyer's advice on the choice of funder or funding contract terms is materially limited by Lawyer's own interests, Lawyer is required to advise Client of the facts and seek Client's informed written consent. Rule 1.7(b). See also, *Santa Clara County Counsel Attys. Assn. v. Woodside* (1994) 7 Cal.4th 525, 546-47 [28 Cal.Rptr.2d 617] (lawyer must evaluate whether the relationship creates a "situation in which [he or she] might compromise his or her representation in order to advance the attorney's own financial or personal interests"). Indeed, Lawyer owes Client a duty to communicate material facts concerning the representation. Rule 1.4. Lawyer's existing relationship with Funder is a material fact. In addition to obtaining informed written consent, rule 1.7(d) requires that Lawyer reasonably believe that Lawyer can provide Client with diligent and competent representation notwithstanding the rule 1.7(b) conflict.

Rule 1.8.1 applies where a lawyer obtains a pecuniary (financial) interest *adverse to the client*. There is nothing adverse to a client about a lawyer getting paid for legal services. See Cal. State Bar Formal Opn. No. 2002-159, n.3 ("Although the lawyer does receive some benefit from the escrow arrangement—she is assured that there are funds available to pay her fees and costs–this is no different from the benefit the lawyer receives by requiring an advance fee and placing it in her trust account. The lawyer, by requiring an advanced fee, does not thereby come within rule 3-300."). Thus, the rule does not apply merely because the arrangement permits a lawyer to get paid its fees. On the other hand, if a lawyer owns a share in the litigation funding company, the funding arrangement would constitute a business transaction with the client and the lawyer would be obliged to comply with rule 1.8.1.

Scenario 3

This is the same as the prior scenario, except that Funder pays Lawyer's legal fees directly for the representation of Client.

Lawyer must not enter into an agreement, charge, or accept compensation for representing Client in this scenario, unless Lawyer ensures that: (1) there is no interference with Lawyer's independent professional judgment or relationship with Client, (2) the information is protected as required by Business and Professions Code section 6068(e)(1) and rule 1.6, and (3) Lawyer obtains Client's informed written consent as set forth in rule 1.8.6(c). Rule 1.8.6(a)-(c).

Lawyer must also ensure that such a payment arrangement does not interfere with Lawyer's obligation to render candid advice and exercise of independent professional judgment under rule 2.1. As for the informed written consent required in this scenario, Lawyer must communicate and explain (i) the relevant circumstances; and (ii) the material risks, including any actual and reasonably foreseeable adverse consequences of the proposed course of conduct. See rule 1.0.1(e) (defining informed consent).

Moreover, rule 1.8.6 does not alter or diminish a lawyer's obligations under rule 5.4(c), which addresses financial arrangements with third parties. Rule 1.8.6, Comment [5]. In other words, in such a payment arrangement it remains paramount that Lawyer not permit the third-party payor to direct or regulate Lawyer's independent professional judgment or interfere with the attorney-client relationship.

F. Impact on Attorney's Duty of Confidentiality

According to the facts of Scenario 2, Lawyer shares a legal analysis memo with Funder after Funder signed an NDA. Lawyer also engages in communications with Funder about the progress of the case. These activities implicate Lawyer's ethical obligation to maintain the confidentiality of information learned in the course of the representation and to apply diligence, learning and skill to avoid adverse consequences, such as a waiver of privileges and protections to which the clients is entitled.

Case law concerning whether funding agreements and communications with funders are privileged is still developing. Most but not all courts that have considered the question have held that work product does not lose its work product status because an attorney or client shares that work product with a funder either orally or in writing.[7/] That is because work-

[7/] See, e.g., *Miller UK Ltd. v. Caterpillar, Inc*. (N.D. Ill. 2014) 17 F.Supp.3d 711, 738 (holding that sharing with funder did not waive work product because disclosure did not substantially increase the likelihood that an adversary would obtain the materials where claimant had oral and written confidentiality agreements with prospective and actual funders); but see *Leader Technologies, Inc. v. Facebook, Inc*. (D. Del. 2010) 719 F.Supp.2d 373, 376-77 (work product protection waived by sharing with funder). See also DeStefano, *Claim Funders and Commercial Claim Holders: A Common Interest or a Common Problem?* (2014) 63 DePaul L.Rev. 305 (favoring common interest attorney-client privilege and work product

product protection is only subject to waiver based on disclosure to a third-party where the disclosure "substantially increase[es] the possibility that an opposing party will obtain the information." 2 Mueller & Kirkpatrick, *Federal Evidence* (4th ed. 2016) § 5:38; see also *Laguna Beach County Water Dist. v. Superior Court* (2004) 124 Cal.App.4th 1453, 1459 [22 Cal.Rptr.3d 387] (disclosure operates as a waiver only where the otherwise protected information is divulged to someone with no interest in maintaining confidentiality). Taking steps to ensure that the funder will keep all information it receives confidential such as by entering into a confidentiality agreement and/or marking documents appropriately will decrease the risk that a court will find that work product is waived. Such steps are therefore consistent with Lawyer's ethical duty to safeguard confidential information. However, particularly because case law is still developing, Lawyer should also inform Client of the risks of waiver and obtain the Client's consent. See rule 1.6(a) (lawyer may not reveal client confidences without informed written consent in this context).

Under Scenario 2, Lawyer communicates frequently with the Funder about the case. Lawyer has an obligation to consider whether such communications may be discoverable, advise Client as to any risk of discoverability, take steps necessary to minimize the risk and ensure that the Client consents to disclosure. The few courts that have considered whether involving a funder in attorney-client privileged communications waives the privilege have split on the issue. Some courts, for example, have accepted the argument that such communications are protected from waiver by the common interest exception because the funder and client share a common legal goal.[8/]

Finally, throughout the litigation, Lawyer must not allow the relationship with Funder to impair Lawyer's objectivity and loyalty to Client. Lawyer must remain cognizant that the company is the Client, not the Funder.

CONCLUSION

Opportunities exist to contract with litigation funders. Attorneys who represent clients that consider or take these opportunities must be cognizant of ethical considerations that are implicated. The lawyer is obliged to provide independent professional judgment not shaded by a third-party with an interest in the outcome of the litigation. The lawyer must ensure

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protection for collaborative work and communications between funders and claim holders); Giesel, *Alternative Litigation Finance and the Work–Product Doctrine* (2012) 47 Wake Forest L.Rev. 1083 (concluding that the involvement of alternative litigation financing entities in litigation should not affect work product privilege and materials evaluating litigation should enjoy protection).

[8/] Compare *In re International Oil Trading Co., LLC* (S.D. Fl. 2016) 548 B.R. 825 [62 Bankr.Ct.Dec. 145] (communications between funder, claimant and counsel protected by the attorney client privilege and the common interest exception to waiver as well as agency exception) with *Miller UK Ltd. v. Caterpillar, Inc*. (N.D. Ill. 2014) 17 F.Supp.3d 711, 738 (a client's relationship to a litigation funder was merely "a shared rooting interest in the 'successful outcome of a case'" and thus "not a common legal interest").

competence in advising on litigation funding including staying abreast of relevant law, such as whether disclosures to funders waive any evidentiary protections. The lawyer must obtain the client's informed consent before providing any client confidential information.

124 F.4th 140
United States Court of Appeals, Second Circuit.

E. Jean CARROLL, Plaintiff-Appellee,

v.

Donald J. TRUMP, Defendant-Appellant.

Docket No. 23-793-cv
|
August Term 2024
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Argued: September 6, 2024
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Decided: December 30, 2024

Synopsis

Background: Author sued former President of the United States after passage of the New York Adult Survivors Act (ASA), seeking damages based on allegations that he had sexually assaulted her years earlier, when he was a private businessman, and bringing a defamation claim based on former President's statements made on a social-media website after he left office and after she filed suit in which he denied her sexual-assault allegations, called her lawsuit a "con job," and accused her of "not telling the truth." The United States District Court for the Southern District of New York, Lewis A. Kaplan, J., 650 F. Supp. 3d 213, denied former President's motions to dismiss and, before trial, 2023 WL 3000562, denied former President's motion in limine and, 2023 WL 2652636, granted in part and denied in part author's motion in limine. After a jury found former President liable under New York law for both sexual abuse and defamation and awarded author $5 million in compensatory and punitive damages, the District Court, Kaplan, J., entered judgment on the jury's verdict and, 683 F. Supp. 3d 302, denied former President's motion for a new trial on damages or a remittitur. Former President appealed, challenging evidentiary rulings below and seeking a new trial.

Holdings: The Court of Appeals held that:

as a matter of first impression, in determining in a sexual-assault case whether to admit evidence of another sexual assault by the defendant, the trial court must ask, based on all the evidence, whether a jury could reasonably find by a preponderance of the evidence that the other sexual assault occurred;

district court did not commit any error in failing to give jury a limiting instruction stating that evidence of other sexual assaults allegedly committed by former President could be considered only with respect to author's sexual-assault claim, and not to prove her defamation claim;

district court properly admitted testimony of witness who alleged that former President had groped her on an airplane;

district court did not abuse its discretion in admitting testimony of witness who alleged that former President had non-consensually kissed her after inviting her to an unoccupied room in his residence;

district court did not abuse its discretion in admitting recording of former President's statements, made to a television host, about his actions towards women;

district court did not abuse its discretion in excluding extrinsic evidence, and barring cross-examination, about funding of author's litigation expenses;

district court did not err in sustaining author's objection to assertions in former President's opening statement about whether certain attorney had made recommendations about author's choice of counsel;

district court did not err in refusing to admit into evidence a redacted transcript of a conversation between author and witness who testified about having allegedly been sexually assaulted by former President;

district court did not abuse its discretion in barring former President from cross-examining author about her statement with respect to possessing former President's DNA;

district court did not abuse its discretion in limiting questioning by former President about why author had not sought to bring criminal charges;

district court did not abuse its discretion in barring former President from asking author why she had not sought to obtain video-camera footage from store where he had allegedly assaulted her; and

even assuming arguendo that district court erred in some of its evidentiary rulings, no claimed error or combination of errors affected former President's substantial rights.

Affirmed.

See also 660 F. Supp. 3d 196.

***149** ON APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF NEW YORK (Lewis A. Kaplan, *Judge*)

Attorneys and Law Firms

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D. John Sauer, James Otis Law Group, LLC, St. Louis, MO, and Todd Blanche and Emil Bove, Blanche Law, New York, NY, on the brief, for Defendant-Appellant.

Before: Chin, Carney, and Pérez, Circuit Judges.

Opinion

Per Curiam:

***150** In this case, after a nine-day trial, a jury found that plaintiff-appellee E. Jean Carroll was sexually abused by defendant-appellant Donald J. Trump at the Bergdorf Goodman department store in Manhattan in 1996. The jury also found that Mr. Trump defamed her in statements he made in 2022. The jury awarded Ms. Carroll a total of $5 million in compensatory and punitive damages.

Mr. Trump now appeals, contending that the district court (Lewis A. Kaplan, *Judge*) erred in several of its evidentiary rulings. These include its decisions to admit the testimony of two women who alleged that Mr. Trump sexually assaulted them in the past and to admit a recording of part of a 2005 conversation in which Mr. Trump described to another man how he kissed and grabbed women without first obtaining their consent. Mr. Trump contends that these and other asserted errors entitle him to a new trial.

On review for abuse of discretion, we conclude that Mr. Trump has not demonstrated that the district court erred in any of the challenged rulings. Further, he has not carried his burden to show that any claimed error or combination of claimed errors affected his substantial rights as required to warrant a new trial.

Accordingly, and for the reasons set forth more fully below, we AFFIRM the judgment of the district court.

BACKGROUND

On appeal from a jury verdict, the court of appeals is bound to "construe all evidence, draw all inferences, and make all credibility determinations in favor of the party [who] prevailed before the jury." *Jia Sheng v. M&TBank Corp.*, 848 F.3d 78, 81 (2d Cir. 2017) (quoting *DiBella v. Hopkins*, 403 F.3d 102, 110 (2d Cir. 2005)). Here, that party is Ms. Carroll. We describe the narrative heard by the jury accordingly. Mr. Trump did not testify at trial but has denied the allegations that he engaged in any sexual misconduct with Ms. Carroll and that he defamed her.

I. *The Evidence Presented at Trial*

We summarize the evidence presented to the jury regarding the charged 1996 assault and 2022 defamation of Ms. Carroll.

A. *The Bergdorf Goodman Assault*

In 1996, Ms. Carroll encountered Mr. Trump at the Bergdorf Goodman department store in Manhattan. At the time, Ms. Carroll was an advice columnist for Elle Magazine and hosted a daily advice talk show called "Ask E. Jean." App'x at 1570-73. Mr. Trump recognized Ms. Carroll and asked her to stay and help him pick a gift for a girl. Describing this as a "funny New York scene" and a "wonderful prospect" for a "born advice columnist" to give advice to Mr. Trump on buying a gift, Ms. Carroll said yes. *Id.* at 1590.

After Ms. Carroll suggested that Mr. Trump purchase a handbag or a hat, Mr. Trump proposed that they go to the lingerie department instead. Ms. Carroll and Mr. Trump went to the lingerie department on the sixth floor. Mr. Trump selected a piece of lingerie and insisted that Ms. Carroll try it on. Ms. Carroll jokingly responded, ***151** "You put it on. It's your color." *Id.* at 1595. After some playful banter, Mr. Trump took Ms. Carroll's arm and motioned for her to go to the dressing room with him. Because Mr. Trump was being "very light" and "pleasant" and "funny," *id.* at 1595, Ms. Carroll walked with Mr. Trump into the open dressing room, which she described as "sort of an open area," *id.* at 1596. But as

soon as she entered, Mr. Trump "immediately shut the door" and "shoved [her] against the wall ... so hard [that] [her] head banged." *Id.*

Ms. Carroll pushed Mr. Trump back, but "he thrust [her] back against the wall again," causing her to "bang[ ] [her] head again." *Id.* at 1597. With his shoulder and the whole weight of his body against her, Mr. Trump held her against the wall, kissed her, pulled down her tights, and stuck his fingers into her vagina -- until Ms. Carroll managed to get a knee up and push him back off of her. [1] She immediately "exited the room" and left the store "as quickly as [she] could." *Id.* at 1601. The encounter lasted just a few minutes.

Within a day, Ms. Carroll told two friends, Lisa Birnbach and Carol Martin, about the sexual assault. She did not report the incident to the police, however, or share it publicly for over two decades. While conducting interviews for a book that she was writing in 2017, the accounts of assaults perpetrated by Harvey Weinstein came to light and received nationwide attention. As a consequence of the many women who came forward to report their experiences of sexual assault, Ms. Carroll finally decided to share more broadly what Mr. Trump had done to her in 1996.

B. *The Defamation*

In June 2019, *New York* magazine published an excerpt from Ms. Carroll's then-forthcoming book, in which Ms. Carroll wrote that Mr. Trump raped her at the Bergdorf Goodman store in 1996. Mr. Trump denied the allegations and made a series of public statements in which he claimed that Ms. Carroll lied about the sexual assault. Mr. Trump made these statements in 2019 while he was still President of the United States. [2]

About three years later, on October 12, 2022, after he had left office and after Ms. Carroll announced her intentions to sue him for rape and sexual assault, Mr. Trump posted a statement on Truth Social, his social media outlet, under the heading "Statement by Donald J. Trump, 45th President of the United States of America." ***152** *Id.* at 2858. The statement read, in part:

> This "Ms. Bergdorf Goodman case" is a complete con job, and our legal system in this Country, but especially in New York State (just look at Peekaboo James), is a broken disgrace. You have to fight for years, and spend a fortune, in order to get your reputation back from liars, cheaters, and hacks. ... I don't know this woman, have no idea who she is, other than it seems she got a picture of me many years ago, with her husband, shaking my hand on a reception line at a celebrity charity event. She completely made up a story that I met her at the doors of this crowded New York City Department Store and, within minutes, "swooned" her. It is a Hoax and a lie, just like all the other Hoaxes that have been played on me for the past seven years. And, while I am not supposed to say it, I will. This woman is not my type! She has no idea what day, what week, what month, what year, or what decade this so-called "event" supposedly took place. The reason she doesn't know is because it never happened, and she doesn't want to get caught up with details or facts that can be proven wrong. If you watch Anderson Cooper's interview with her, where she was promoting a really crummy book, you will see that it is a complete Scam. ... In the meantime, and for the record, E. Jean Carroll is not telling the truth, is a woman who I had nothing to do with, didn't know, and would have no interest in knowing her if I ever had the chance.

Id. at 2858.

II. *The Proceedings Below*

A. *Carroll I*

In 2019, Ms. Carroll sued Mr. Trump in New York state court, seeking to recover damages for defamation. The case was removed to the U.S. District Court for the Southern District of New York in September 2020. *Carroll v. Trump*, No. 20-cv-07311 (LAK), 2020 WL 13728008 (S.D.N.Y. filed Sept. 8, 2020) ("*Carroll I*"). In *Carroll I*, Ms. Carroll asserted defamation claims against Mr. Trump based on the statements

he made in June 2019, after Ms. Carroll published her account of the alleged rape, when he was still President of the United States. *Carroll I* did not include any damages claim for the alleged rape or sexual assault itself.

Carroll I was delayed due to proceedings concerning Mr. Trump's presidential immunity defense and whether the United States could be substituted as a party for Mr. Trump. *See Carroll v. Trump*, 49 F.4th 759, 761 (2d Cir. 2022) (holding that the President is an "employee of the government" for purposes of the Westfall Act, and certifying to the D.C. Court of Appeals the question of whether Mr. Trump's statements were made within the scope of his employment as President of the United States); *Carroll v. Trump*, 66 F.4th 91, 94 (2d Cir. 2023) (per curiam) (remanding to the district court for further proceedings based on guidance from the D.C. Court of Appeals); *Carroll v. Trump*, 88 F.4th 418, 432 (2d Cir. 2023) (finding no error in the district court's denial, on grounds of undue delay and prejudice, of Mr. Trump's request for leave to amend his answer to raise the defense of presidential immunity).

While *Carroll I* was pending, the State of New York passed the Adult Survivors Act (the "ASA"). N.Y. C.P.L.R. § 214-j (McKinney 2022). The ASA provided adult victims of sexual abuse with a new one-year window in which to sue their abusers, even if an otherwise applicable statute of limitations had previously expired. *Id.* In August 2022, Ms. Carroll advised the district ***153** court that she intended to sue Mr. Trump for damages for the alleged rape once the ASA's filing window opened, on November 24, 2022. Letter from Roberta A. Kaplan to Hon. Lewis A. Kaplan, *Carroll I*, Dkt. No. 89 at 3 (filed Sept. 20, 2022).

B. *Carroll II*

On November 24, 2022, three years after she initiated *Carroll I*, and minutes after the ASA's authorization to file new claims became effective, Ms. Carroll filed a second action against Mr. Trump -- the case now before us on appeal. *Carroll v. Trump*, No. 22-cv-10016 (LAK), 2022 WL 19826795 (S.D.N.Y. filed Nov. 24, 2022) ("*Carroll II*"). Unlike the first action, which was based solely on Mr. Trump's statements made while he was still in office, *Carroll II* sought damages for the alleged rape itself as well as for the purportedly defamatory statements made by Mr. Trump on October 12, 2022, after he left office.

In *Carroll II*, the district court ruled on a number of evidentiary issues in a series of written opinions issued before trial. Relevant to the instant appeal, the district court ruled that two witnesses, Jessica Leeds and Natasha Stoynoff, would be permitted to testify about other incidents of alleged sexual misconduct by Mr. Trump, and that the *Access Hollywood* tape -- a recording of a 2005 conversation involving Mr. Trump -- was admissible. *Carroll v. Trump*, 660 F. Supp. 3d 196, 202-08 (S.D.N.Y. 2023) (ruling on other acts evidence in *Carroll I*); *see also Carroll v. Trump*, No. 22-cv-10016 (LAK), 2023 WL 3000562, at *1 & n.4 (S.D.N.Y. Mar. 20, 2023) (incorporating *Carroll v. Trump*, 660 F. Supp. 3d 196 (S.D.N.Y. 2023)); *Carroll v. Trump*, No. 22-cv-10016 (LAK), 2023 WL 2652636, at *8 (S.D.N.Y. Mar. 27, 2023) (making additional evidentiary rulings). The district court also precluded any reference to DNA evidence or Ms. Carroll's choice of counsel. *Carroll*, 2023 WL 2652636, at *5-8.

Trial in *Carroll II* commenced on April 25, 2023, and concluded on May 8, 2023. Ms. Carroll testified for nearly three days -- almost two full days of which consisted of cross-examination. Ms. Carroll called two "outcry witnesses" -- Lisa Birnbach and Carol Martin -- who each testified that Ms. Carroll told them about the attack by Mr. Trump shortly after it occurred. Ms. Carroll also called Ms. Leeds and Ms. Stoynoff, who testified as set forth below, as well as two witnesses who were employed at Bergdorf Goodman at the time of the assault. The latter testified as to the layout of the store and presence or absence of surveillance cameras and personnel. The jury also watched the *Access Hollywood* tape twice. Ms. Carroll also called a clinical psychologist and a professor of marketing. Mr. Trump did not testify in person, and did not attend the trial. The jury did, however, watch portions of Mr. Trump's videotaped October 2022 deposition testimony.

On May 9, 2023, the nine-person jury unanimously found that Mr. Trump had "sexually abused" Ms. Carroll in 1996. [3] Jury Verdict Form, *Carroll II*, Dkt. 174. *See also Carroll v. Trump*, 683 F. Supp. 3d 302, 307 (S.D.N.Y. 2023) ("[T]he jury implicitly found that Mr. Trump deliberately and forcibly penetrated Ms. Carroll's vagina with his fingers."). The jury found that Ms. Carroll was injured as a result of Mr. Trump's conduct and awarded her $2 million in compensatory damages and $20,000 in punitive damages. The jury also found ***154** that Mr. Trump defamed Ms. Carroll and awarded her $2.7 million in compensatory damages and $280,000 in punitive damages. Accordingly, the jury awarded Ms. Carroll a total of $5 million. Judgment was entered on May 11, 2023. Mr. Trump filed a notice of appeal the same day.

Mr. Trump thereafter moved for a new trial. In a fifty-nine-page memorandum opinion filed July 19, 2023, the district court denied the motion. *Carroll*, 683 F. Supp. 3d at 334. Mr. Trump filed an amended notice of appeal the same day. [4]

DISCUSSION

I. *Applicable Law*

On appeal, Mr. Trump focuses on evidentiary rulings that he argues were erroneous. We begin our review by summarizing the law with respect to (a) the admissibility under the Federal Rules of Evidence of evidence of other sexual assaults; (b) the proper application of Rule 404(b) of the Federal Rules of Evidence; and (c) the standard of review on appeal from a district court's evidentiary rulings.

A. *Evidence of Other Sexual Assaults*

Rule 415 of the Federal Rules of Evidence provides that "[i]n a civil case involving a claim for relief based on a party's alleged sexual assault ... the court may admit evidence that the party committed any other sexual assault." Fed. R. Evid. 415(a). "The evidence may be considered as provided in Rules 413 and 414." *Id.*

In turn, Rule 413 defines "sexual assault" as a "crime under federal law or under state law" involving:

> (1) any conduct prohibited by 18 U.S.C. chapter 109A;
>
> (2) contact, without consent, between any part of the defendant's body -- or an object -- and another person's genitals or anus;
>
> (3) contact, without consent, between the defendant's genitals or anus and any part of another person's body;
>
> (4) deriving sexual pleasure or gratification from inflicting death, bodily injury, or physical pain on another person; or
>
> (5) an attempt or conspiracy to engage in conduct described in subparagraphs (1)-(4).

Fed. R. Evid. 413(d).

Rules 413 and 415, together with Rule 414, are congressionally-enacted exceptions to the "general ban against propensity evidence." *United States v. Schaffer*, 851 F.3d 166, 177 (2d Cir. 2017) (internal quotation marks omitted). Thus, "[u]nlike Federal Rule of Evidence 404(b), which allows prior bad act evidence to be used for purposes *other than* to show a defendant's propensity to commit a particular crime," *id*. at 177 (emphasis in original), Rules 413 and 415 permit a jury to consider evidence of a different sexual assault "precisely to show that a defendant has a *pattern or propensity for committing sexual assault*," *id*. at 178 (emphasis added). *See also id*. at 177-78 ("Rule 413 permits the jury to consider the evidence 'on any matter to which it is relevant.' " (quoting Fed. R. Evid. 413(a))).

Congress "considered knowledge that the defendant has committed [sexual assault] on other occasions to be critical in assessing the relative plausibility of sexual assault claims and accurately deciding ***155** cases that would otherwise become unresolvable swearing matches." *Id.* at 178 (alterations adopted) (internal quotation marks omitted). "[T]he practical effect of Rule 413 [and Rules 414 and 415] is to create a presumption that evidence of prior sexual assaults is relevant and probative" in cases based on sexual assault. *Id.* at 180. [5]

Rule 403's protections apply to evidence being offered under Rule 415. *Id.* Accordingly, if the trial court finds that the other act evidence is admissible under Rules 413 and 415, it may still exclude the evidence if it finds that the probative value of the propensity evidence is "substantially outweighed by a danger of ... unfair prejudice, confusing the issues, misleading the jury, undue delay, wasting time, or needlessly presenting cumulative evidence." Fed. R. Evid. 403.

Rules 413 and 415 are silent as to the standard that courts should apply in determining whether to admit evidence of past sexual assaults. Both parties accept the district court's legal conclusion that the standard articulated by the Supreme Court in *Huddleston v. United States*, 485 U.S. 681, 108 S.Ct. 1496, 99 L.Ed.2d 771 (1988), to determine the admissibility of Rule 404(b) evidence is also the appropriate standard for admitting evidence under Rules 413-415. *Huddleston* teaches that "the trial court neither weighs credibility nor makes a finding that the [party seeking admission] has proved the conditional fact by a preponderance of the evidence." *Id*. at 690, 108 S.Ct. 1496. Rather, the "court simply examines all the evidence in the case and decides whether the jury could reasonably find the conditional fact -- whether the defendant committed the prior act -- by a preponderance of the evidence." *Johnson v. Elk Lake Sch. Dist.*, 283 F.3d 138, 152 (3d Cir. 2002) (alteration adopted) (quoting *Huddleston,* 485 U.S. at 690, 108 S.Ct. 1496).

We have not had occasion to decide this question. Most of our sister circuits, including the Third, Fourth, Sixth, Eighth, Ninth, and Tenth, have employed the *Huddleston* standard as the standard for admitting evidence under Rules 413, 414, or 415. *See Johnson*, 283 F.3d at 154-55; *United States v. Fitzgerald*, 80 F. App'x 857, 863 (4th Cir. 2003); *United States v. Hruby*, 19 F.4th 963, 966-67 (6th Cir. 2021); *United States v. Oldrock*, 867 F.3d 934, 938 (8th Cir. 2017); *United States v. Norris*, 428 F.3d 907, 913-14 (9th Cir. 2005); *United States v. Enjady*, 134 F.3d 1427, 1433 (10th Cir. 1998).

We agree with our sister circuits and join them in holding that the *Huddleston* standard for admitting evidence applies to Rule 415. We reach this conclusion based on relevant textual similarities between Rule 404(b) and Rules 413-415 and their respective legislative histories. Rule 404(b) and Rules 413-415 all permit the introduction of evidence of other bad acts, including uncharged conduct. [6] Moreover, the ***156** text of Rules 413-415, like the text of Rule 404(b), "contains no intimation ... that any preliminary showing is necessary before ... evidence may be introduced for a proper purpose." *Huddleston*, 485 U.S. at 687-88, 108 S.Ct. 1496 (holding that no preliminary finding is required under Rule 404(b)). The legislative history behind Rules 413-415, like that behind Rule 404(b), also weighs against requiring a preliminary preponderance finding by the court that the other sexual assault occurred. *See id.* at 688-89, 108 S.Ct. 1496. [7] Accordingly, in determining whether to admit other sexual act evidence, the trial court need not itself find by a preponderance of the evidence that the other assault occurred. Instead, the court must "ask whether a jury could reasonably make such a finding." *Johnson*, 283 F.3d at 152 (internal quotation marks omitted).

In sum, in addition to other requirements not relevant here, the district court may admit evidence of other sexual assaults under Rule 415 when: (1) the civil case before it involves a claim for relief based on a party's alleged sexual assault; (2) the court determines that a jury could reasonably find by a preponderance of the evidence that the party committed the other sexual assault (as defined by Rule 413); and (3) applying Rule 403, the court further determines that the probative value of the evidence is not substantially outweighed by the danger of unfair prejudice.

B. ***Rule 404(b)***

While Rules 413 and 415 permit propensity evidence in sexual assault cases, the usual rule is that propensity evidence is not allowed. Rule 404(b) of the Federal Rules of Evidence governs the admissibility of other act evidence -- that is, "any ... crime, wrong, or act" other than those charged. Fed. R. Evid. 404(b)(1). Evidence of other acts is not admissible if offered "to prove a person's character in order to show that on a particular occasion the person acted in accordance with the character." *Id.* Such evidence may be admissible, however, if offered "for another purpose." *Id.* 404(b)(2). Acceptable purposes include, but are not limited to, showing "motive, opportunity, intent, preparation, plan, knowledge, identity, absence of mistake, or lack of accident." *Id.*; *see also* 1 McCormick, Evidence § 190.1 (8th ed. 2020) (recognizing that evidence of other acts "may be used in numerous ways, and those enumerated [in Rule 404(b)] are neither mutually exclusive nor collectively exhaustive"). Other acceptable purposes include providing direct corroboration of other testimony, *see United States v. Everett*, 825 F.2d 658, 660-61 (2d Cir. 1987), and showing the existence of a ***157** pattern, or "*modus operandi*," which may be relevant "to prove that the actor possessed the required mental state (*mens rea*), or to prove the charged act occurred (*actus reus*)." David P. Leonard, *New Wigmore: A Treatise on Evidence: Evidence of Other Misconduct and Similar Events* § 13.3 (2d ed. 2020).

This Court has long taken an "inclusionary" approach to Rule 404(b), under which other act evidence is admissible unless it is introduced for the sole purpose of showing a defendant's bad character, subject to the relevance and prejudice considerations set out in Rules 402 and 403. *United States v. Pascarella*, 84 F.3d 61, 69 (2d Cir. 1996); *Ismail v. Cohen*, 899 F.2d 183, 188 (2d Cir. 1990); *see also United States v. Robinson*, 702 F.3d 22, 37 (2d Cir. 2012) (evidence of uncharged criminal conduct that "is inextricably intertwined with the evidence regarding the charged offense, or ... necessary to complete the story of the crime on trial," is not typically excluded under Rule 404(b) (citation omitted)).

"To determine whether a district court properly admitted other act evidence, the reviewing court considers whether (1) it was offered for a proper purpose; (2) it was relevant to a material issue in dispute; (3) its probative value is substantially outweighed by its prejudicial effect; and (4) the trial court gave an appropriate limiting instruction to the jury if so requested by the defendant." *United States v. LaFlam*, 369 F.3d 153, 156 (2d Cir. 2004).

C. ***Review of Evidentiary Rulings***

We review a district court's evidentiary rulings for "abuse of discretion." *Schaffer*, 851 F.3d at 177. Abuse of discretion is a term of art that "merely signifies that a district court based its ruling on an erroneous view of the law or on a clearly erroneous assessment of the evidence, or rendered a decision that cannot be located within the range of permissible decisions." *Vill. of Freeport v. Barrella*, 814 F.3d 594, 611 (2d Cir. 2016) (internal quotation marks omitted). A district court's legal interpretation of the Federal Rules of Evidence is reviewed *de novo*. *See United States v. Samet*, 466 F.3d 251, 254 (2d Cir. 2006). We accord "great deference" to a district court, however, in ruling "as to the relevancy and unfair prejudice of proffered evidence, mindful that it sees the witnesses, the parties, the jurors, and the attorneys, and is thus in a superior position to evaluate the likely impact of the evidence." *United States v. Paulino*, 445 F.3d 211, 217 (2d Cir. 2006) (internal quotation marks omitted).

We "will disturb an evidentiary ruling only where the decision to admit or exclude evidence was manifestly erroneous." *United States v. Litvak*, 889 F.3d 56, 67 (2d Cir. 2018) (internal quotation marks omitted). "To find such abuse [of discretion], we must conclude that the trial judge's evidentiary rulings were arbitrary and irrational." *Paulino*, 445 F.3d at 217 (internal quotation marks omitted).

Moreover, even if an evidentiary ruling is manifestly erroneous, we will affirm and not require a retrial if we conclude that the error was harmless. *Cameron v. City of New York*, 598 F.3d 50, 61 (2d Cir. 2010); *see also United States v. Siddiqui*, 699 F.3d 690, 702 (2d Cir. 2012). "[A]n erroneous evidentiary ruling warrants a new trial only when 'a substantial right of a party is affected,' as when 'a jury's judgment would be swayed in a material fashion by the error.' " *Lore v. City of Syracuse*, 670 F.3d 127, 155 (2d Cir. 2012) (quoting *Arlio v. Lively*, 474 F.3d 46, 51 (2d Cir. 2007)). Thus, "[a]n error is harmless if we can conclude with fair assurance that the evidence did not substantially influence ***158** the jury." *Cameron*, 598 F.3d at 61 (internal quotation marks omitted). "In civil cases, the burden falls on the appellant to show that the error was not harmless and that 'it is likely that in some material respect the factfinder's judgment was swayed by the error.' " *Warren v. Pataki*, 823 F.3d 125, 138 (2d Cir. 2016) (quoting *Tesser v. Bd. of Educ. of City Sch. Dist.,* 370 F.3d 314, 319 (2d Cir. 2004)); *see also Tesser,* 370 F.3d at 319 ("An erroneous evidentiary ruling that does not affect a party's 'substantial right' is ... harmless.").

Evidentiary objections not raised in the district court are reviewed for plain error only. *Cruz v. Jordan*, 357 F.3d 269, 271 (2d Cir. 2004). Under that standard, "there must be (1) error, (2) that is plain, and (3) that affects substantial rights." *United States v. Gomez*, 705 F.3d 68, 75 (2d Cir. 2013) (alteration adopted) (internal quotation marks omitted). "If all three conditions are met, an appellate court may then exercise its discretion to notice a forfeited error, but only if (4) the error seriously affects the fairness, integrity, or public reputation of judicial proceedings." *Id.* (alteration adopted) (internal quotation marks omitted); *accord Yukos Capital S.A.R.L. v. Feldman*, 977 F.3d 216, 237 (2d Cir. 2020).

II. *Application*

Mr. Trump's challenges to the district court's evidentiary rulings fall into two categories -- evidence that he contends was erroneously admitted on the one hand, and evidence that he asserts was erroneously precluded on the other. We address each category of evidence and then turn to the question of whether Mr. Trump has carried his burden to show error of such impact that a new trial is warranted.

A. *Admitted Evidence*

We first address Mr. Trump's argument that the defamation claim is not "based on" an alleged sexual assault and that therefore Rule 415 does not apply. We then consider the admissibility of the testimony of Jessica Leeds and Natasha Stoynoff, and the admissibility of the *Access Hollywood* tape.

1. *The Basis of the Claims*

At the outset, on *de novo* review of this legal question, we reject Mr. Trump's assertion that the district court erred in admitting the other acts evidence because, he contends, Ms. Carroll's defamation claim was not " 'based on' sexual assault." Appellant's Br. at 20-21. Mr. Trump's argument misconstrues Rule 415's text and ignores its plain meaning. Again, Rule 415(a) permits evidence of other sexual assaults to be introduced in "civil *case[s]* involving a *claim* for relief *based on* a party's alleged sexual assault." Fed. R. Evid. 415(a) (emphasis added). It is beyond dispute that Ms. Carroll's first claim -- for recovery of damages arising from Mr. Trump's alleged rape of her in 1996 -- is "based on" a sexual assault. *Id.* Mr. Trump does not argue otherwise on appeal. Thus, *Carroll II* is a civil case that involves a claim for relief based on a party's alleged sexual assault.

Instead, Mr. Trump argues that the jury should not have been permitted to consider evidence admitted pursuant to Rule 415(a) when considering Ms. Carroll's second claim, for recovery of damages arising from the alleged defamation. But he does not identify any case law holding that Rule 415 evidence is admissible *only* to prove sexual assault claims. Indeed, the text of the rule contains no such limitation.

Because Mr. Trump acknowledges that Ms. Carroll's sexual assault claim was "based on" a sexual assault, we understand ***159** his argument really to be that the evidence was not admissible to prove the defamation claim. In other words, Mr. Trump is arguing that the district court should have given the jury a limiting instruction, advising that it could consider the other sexual assault evidence only with respect to the sexual assault claim and not with respect to the defamation claim.

But Mr. Trump failed to raise this contention below.[8] Therefore, we review the absence of a limiting instruction for plain error only. We discern no plain error here. The other act evidence was relevant to Ms. Carroll's defamation claim -- she had to show that she *was* sexually assaulted by Mr. Trump to prove that his assertion that she was engaging in a "[h]oax," App'x at 2858, was false and therefore defamatory.[9] Hence, the evidence was relevant under Rule 401 because it was offered to prove a sexual assault, and it had a tendency to prove that Mr. Trump did sexually assault Ms. Carroll. *See* Fed. R. Evid. 401 ("Evidence is relevant if: (a) it has any tendency to make a fact more or less probable than it would be without the evidence; and (b) the fact is of consequence in determining the action."). Moreover, as discussed, Mr. Trump does not cite any authority for the proposition that Rule 415 evidence is admissible only to prove a sexual assault claim, even where, as here, the evidence might otherwise be relevant. *See United States v. Whab*, 355 F.3d 155, 158 (2d Cir. 2004) (observing that it is "exceedingly rare" to find plain error "in the absence of binding precedent").

For these reasons, we conclude that the district court did not err, much less plainly err, in permitting the jury to consider this evidence with respect to Ms. Carroll's defamation claim.

2. *The Admissibility of the Evidence of Other Sexual Assaults*

We next turn to whether the district court abused its discretion in admitting the other sexual assaults evidence -- the testimony of Jessica Leeds and Natasha Stoynoff and the *Access Hollywood* recording -- and we conclude that it did not.

a. *The Leeds Testimony*

Jessica Leeds testified that she was on an airplane flying to New York in 1978 or 1979 when a flight attendant came down the aisle to ask if she "would like to come up to first class." App'x at 2098-99. Welcoming the invitation, Ms. Leeds went up to first class where she sat down next to a man sitting at the window who introduced himself as Donald Trump. The two chatted. After their meal was served and cleared, however, Mr. Trump suddenly "decided to kiss [her] and grope [her]." *Id.* at 2101. Ms. Leeds testified at trial:

> [I]t was like a tussle. He was -- his hands and -- he was trying to kiss me, he was trying to pull me towards him. He was grabbing my breasts, he was -- it's like he had 40 zillion hands, and it was a tussling match between the two of us. And it was when he started putting his hand up my skirt that that kind of gave me a jolt of strength, and I managed ***160** to wiggle out of the seat and I went storming back to my seat in the coach.

Id. at 2101-02.

On cross-examination, Ms. Leeds further explained:

> Q: OK. And then according to you he, at one point, put his hand on your knee?
>
> A: He started putting his hand up my skirt.
>
> Q: OK, on your leg and up your skirt?
>
> A: Correct.

Id. at 2132. And on re-direct, she explained why she got so upset:

> A: [M]en ... would frequently pat you on the shoulder and grab you or

> something like that and you just -- it is not that serious and you don't -- you don't -- *but when somebody starts to put their hand up your skirt, you know they're serious and this is not good*.

Id. at 2147 (emphasis added).

Mr. Trump argues that Rule 415 does not apply to Ms. Leeds's testimony. He contends that: (1) even if the jury were to credit Ms. Leeds's testimony, she did not describe conduct that constituted a crime at the time the conduct occurred, as Mr. Trump asserts is required under Rule 413(d); (2) no jury could reasonably find that Mr. Trump attempted to bring his body into contact with Ms. Leeds's genitals, as required for admission under Rule 413(d)(2) and (d)(5); and (3) the conduct described by Ms. Leeds could not have been "prohibited" by 18 U.S.C. chapter 109A, as required for admission under Rule 413(d)(1), because (he argues) it did not occur within the requisite federal jurisdiction.

We conclude that the Leeds testimony was properly admitted. First, Mr. Trump's alleged conduct toward Ms. Leeds was a federal crime at the time it occurred. Second, the Leeds testimony was admissible on the ground that Ms. Leeds testified to an "attempt" under Rule 413(d)(5) to engage in the conduct described in Rule 413(d)(2). Fed. R. Evid. 413. And because we conclude that the Leeds testimony was admissible under Rule 413(d)(2) and (d)(5), we do not reach Mr. Trump's Rule 413(d)(1) jurisdiction-based argument here. [10]

We begin with the requirement that the other act be a crime under federal or state law. Mr. Trump argues that the alleged act had to constitute a crime at the time it was committed to satisfy Rule 413(d). We need not decide the issue here because the alleged act clearly was a crime at the time. In 1978 and 1979, just as it is now, it was a federal crime to commit a simple assault on an airplane. And on this record a jury could have reasonably found that Mr. Trump committed a simple assault against Ms. Leeds.

In 1978 and 1979, the law provided, in relevant part:

> Whoever, while aboard an aircraft within the special aircraft jurisdiction of the United States, commits an act which, if committed within the special maritime and territorial jurisdiction of the United States, as defined in section 7 of title 18, would be in violation of section 113 ... of such title 18 shall be punished as provided therein.

49 U.S.C. § 1472(k)(1) (1976). Section 1472(k)(1) thus included as an offense within the "special aircraft jurisdiction of the United States" the conduct proscribed by 18 U.S.C. § 113(e) (1976) -- a simple ***161** assault. In 1978 and 1979, the "special aircraft jurisdiction" extended to any aircraft "within the United States" "while that aircraft is in flight." 49 U.S.C. § 1301(34) (1976); *see also* 49 U.S.C. § 1301(38) (Supp. III 1980). [11]

Ms. Leeds testified that the departure and arrival destinations of the flight in this case were both within the United States, [12] and that Mr. Trump's alleged conduct toward her occurred after the plane had departed, that is, while the plane was "in flight." Moreover, a jury could reasonably find by a preponderance of the evidence that Mr. Trump committed a simple assault by grabbing Ms. Leeds's breasts, kissing her, and pulling her toward him, all without her consent. *See United States v. Delis*, 558 F.3d 177, 184 (2d Cir. 2009) (concluding that simple assault, as governed by section 113 of Title 18, encompassed a "completed common-law battery," which included "offensive touching," and did not require a "specific intent to injure"). [13]

Likewise, we find no error in the trial court's conclusion that a jury could reasonably find by a preponderance of the evidence that Mr. Trump's actions as described by Ms. Leeds qualified as an attempt under (d)(5) to engage in the conduct described in (d)(2). The term "attempt" is not defined in the text of Rule 413. Because Rule 413 deals specifically with "similar crimes in sexual-assault cases," we look to the meaning of the word "attempt" as it is used in federal criminal statutes. *Cf. United States v. Hansen*, 599 U.S. 762, 774-75, 143 S.Ct. 1932, 216 L.Ed.2d 692 (2023) ("[W]hen a criminal-law term is used in a criminal-law statute, that -- in and of itself -- is a good clue that it takes its criminal-law meaning."). In that context, it means having "the intent to commit the crime and engag[ing] in conduct amounting to a substantial step towards the commission of the crime." *United States v. Pugh*, 945 F.3d 9, 20 (2d Cir. 2019) (internal quotation marks omitted). "A substantial step 'is conduct planned to culminate in the commission of the substantive crime being attempted.' " *Id.*

(quoting *United States v. Farhane*, 634 F.3d 127, 147 (2d Cir. 2011)).

Attempt may be found "even where significant steps necessary to carry out the substantive crime are not completed." *Id.* (internal quotation marks omitted). "Because the substantial step need not be the 'last act necessary' before commission of the crime, 'the finder of fact may give ***162** weight to that which has already been done as well as that which remains to be accomplished before commission of the substantive crime.' " *Id.* (quoting *United States v. Manley*, 632 F.2d 978, 987 (2d Cir. 1980)). The behavior "need not be incompatible with innocence, yet it must be necessary to the consummation of the crime ...." *Manley*, 632 F.2d at 987-88. The behavior must also "be of such a nature that a reasonable observer, viewing it in context[,] could conclude beyond a reasonable doubt" -- or in the case of other acts evidence admitted under Rule 415, by a preponderance of the evidence -- "that it was undertaken in accordance with a design to violate the statute." *Id.* at 988.

Ms. Leeds testified that Mr. Trump grabbed her breasts, and tried to kiss her and pull her toward him as she resisted. She also testified unequivocally that Mr. Trump put his hand up her skirt. On the basis of this testimony, a jury could have reasonably found by a preponderance of the evidence that Mr. Trump knowingly took a substantial step toward bringing part of his body -- his hand -- into contact with Ms. Leeds's genitals without her consent. [14]

Other evidence in the case further supports the district court's decision to admit Ms. Leeds's testimony. As discussed below, the jury could reasonably infer from Ms. Stoynoff's testimony and the *Access Hollywood* tape that Mr. Trump engaged in similar conduct with other women -- a pattern of abrupt, nonconsensual, and physical advances on women he barely knew. [15] And, as discussed above, the standard for admitting testimony under Rule 415 -- whether a jury could reasonably find by a preponderance of the evidence that a person committed the attempted assault -- is distinct from and less stringent than the standard for convicting a person criminally of assault or attempted assault, which would have required the jury to make this finding beyond a reasonable doubt.

In sum, the district court did not abuse its discretion in admitting the Leeds testimony at trial.

163 b. *The Stoynoff Testimony

Natasha Stoynoff testified that, in December 2005, when she was a reporter for *People* magazine, she was on assignment at Mar-a-Lago, Mr. Trump's residence in Florida. She was there to do a story about the first anniversary of Mr. Trump's marriage to Melania Trump and the arrival of their son, Barron. Ms. Stoynoff was at Mar-a-Lago for most of the day, conducting interviews of Mr. Trump and his wife between photoshoots. During a break between interviews, Mr. Trump told her that he would like to show her a painting that he had in "this really great room" in the house. App'x at 2349. Mr. Trump then led her to a room in a different part of his residence. Once they arrived at the room, as Ms. Stoynoff described at trial:

> I went in first and I'm looking around, I'm thinking, wow, really nice room, wonder what he wants to show me, and he -- I hear the door shut behind me. And by the time I turn around, he has his hands on my shoulders and he pushes me against the wall and starts kissing me, holding me against the wall.

Id. at 2350. Ms. Stoynoff "tried to push him away," but Mr. Trump came toward her again and she "tried to shove him again." *Id.* at 2350-51. Mr. Trump "was kissing [her]" and "he was against [her] and just holding [her] shoulders back." *Id.* at 2351. The encounter ended when Mr. Trump's butler came into the room. Immediately afterward (Ms. Stoynoff testified), Mr. Trump told her:

> Oh, you know we are going to have an affair, don't you? You know, don't forget what -- don't forget what Marla said, best sex she ever had. We are going to go for steak, we are going to go to Peter Luger's. We're going to have an affair.

Id. at 2352.

Mr. Trump challenges the district court's admission of Ms. Stoynoff's testimony. The district court based its decision to admit the Stoynoff testimony on its finding that it described (1) a crime under Florida law, a proposition that Mr. Trump does not challenge, and (2) an attempt, under Rule 413(d)(5), to engage in conduct described in Rule 413(d)(2).

The trial court did not abuse its discretion when it admitted, pursuant to Rule 413(d)(2) and (5), the evidence of Mr. Trump's alleged actions toward Ms. Stoynoff at Mar-a-Lago in 2005. It found that those actions -- inviting Ms. Stoynoff to an unoccupied room, closing the door behind her, and immediately engaging in nonconsensual kissing despite Ms. Stoynoff's resistance -- suggested a premeditated plan to "take advantage of [the] privacy and to do so without regard to Ms. Stoynoff's wishes." *Carroll*, 660 F. Supp. 3d at 206. We agree and further conclude that the jury could have reasonably found that Mr. Trump took a "substantial step" toward the completion of this premeditated plan when he allegedly closed the door, forcefully held Ms. Stoynoff against the wall while kissing her, and repeatedly came toward her despite being pushed back twice. Mr. Trump's comments to Ms. Stoynoff immediately after the encounter -- including "you know we are going to have an affair" and suggesting they would have the "best sex" -- also shed light on the intent behind his actions. App'x at 2352. That the alleged assault showed no signs of terminating until a third party interrupted it also supports the conclusion that a jury could have reasonably found that Mr. Trump intended to bring his body into contact with Ms. Stoynoff's genitals and that he took substantial steps toward doing so.

In addition, the evidence could have been admitted as an attempt under Rule 413(d)(5) to engage in the type of conduct ***164** under (d)(1): "any conduct prohibited by 18 U.S.C. chapter 109A." Fed. R. Evid. 413(d)(1). Conduct proscribed by chapter 109A includes to "knowingly engage[ ] in sexual contact with another person without that other person's permission." 18 U.S.C. § 2244(b). The chapter defines "sexual contact" as:

> the intentional touching, either directly or through the clothing, of the genitalia, anus, groin, breast, inner thigh, or buttocks of any person with an intent to abuse, humiliate, harass, degrade, or arouse or gratify the sexual desire of any person.

Id. § 2246(3). A jury could have reasonably found, upon consideration of the circumstances discussed above, that the actions alleged constituted an attempt to knowingly engage in conduct that falls within that definition of making "sexual contact," and to do so without Ms. Stoynoff's permission.

Mr. Trump argues (as he did with respect to the Leeds testimony) that, to be admissible under Rule 413(d)(1), the evidence must meet the jurisdictional requirement of 18 U.S.C. chapter 109A: he contends, in other words, that the conduct must have occurred within the "special maritime and territorial jurisdiction of the United States" or certain custodial facilities to qualify as "conduct prohibited by" chapter 109A. [16] Mr. Trump argues that an act that does not meet the jurisdictional requirement of chapter 109A cannot be "prohibited" by chapter 109A. Appellant's Reply Br. at 2-3. We are not persuaded that Rule 413(d)(1) is so constrained.

Mr. Trump's reading is wholly inconsistent with the rationale advanced in Congress in adopting Rules 413-415, which centered on the *nature* of the other conduct, not the specific location in which the conduct occurred. As the text and structure of Rule 413 make clear, Congress did not intend for Rule 413(d)(1) to apply only to conduct occurring within the "special maritime and territorial jurisdiction of the United States" -- that is, among other places, the high seas, on federally controlled land, or in certain custodial facilities. *See* 18 U.S.C. § 7 (defining "special maritime and territorial jurisdiction of the United States"). Rules 413 and 415 permit the admission of evidence that the defendant "committed any other sexual assault," and Rule 413(d) defines "sexual assault" to include "a crime under federal law or under state law ... involving" any one of five categories of conduct. Clearly, in Rule 413(d)(1), Congress was referring to the nature or types of conduct covered in chapter 109A -- such as aggravated sexual abuse, sexual abuse, sexual abuse of a minor, and abusive sexual contact, 18 U.S.C. §§ 2241, 2242, 2243, 2244 -- without limiting the applicability of Rule 413(d)(1) to the conduct occurring on the high seas, on federally-controlled lands, and in certain custodial facilities.

Several of our sister circuits read the statute as we do, stressing the nature of the conduct and disregarding any jurisdictional element. *See, e.g.*, *United States v. Batton*, 602 F.3d 1191, 1196-98 (10th Cir. 2010) (holding defendant's

prior sexual assault of a boy "falls squarely under Rule 413's definition of sexual assault" because it involved conduct that was "clearly proscribe[d]" by chapter 109A, without regard to whether it occurred within the special maritime and territorial jurisdiction of the United States or a custodial facility); ***165** *Blind-Doan v. Sanders*, 291 F.3d 1079, 1082 (9th Cir. 2002) ("We understand Rule 413 to mean acts proscribed by [chapter 109A], whether or not the acts are committed by federal personnel in federal prisons ...."); *United States v. Blazek*, 431 F.3d 1104, 1109 (8th Cir. 2005) ("Rule 413 does not require that the defendant be charged with a chapter 109A offense, only that the instant offense involve conduct proscribed by chapter 109A."). We fail to see any bearing that the jurisdiction of the offense would have on the probative value of the proffered evidence of sexual assault.

The legislative history of the rules also supports our conclusion. For example, the Congressional Record explains that the definition of sexual assault under Rule 413(d) is intended to "cover[ ] federal and state offenses involving *the types of conduct* prohibited by [chapter 109A]." 137 Cong. Rec. 6031 (1991) (emphasis added). [17] And Congress left no doubt that it adopted Rules 413-415 to allow courts to admit evidence that a "defendant has the motivation or disposition to commit sexual assaults." *Id*. The above legislative history confirms that Rule 413(d)(1) hinges on the "type of conduct" alleged, not where the conduct occurred. *See also United States v. Sturm*, 673 F.3d 1274, 1283 (10th Cir. 2012) (analyzing legislative history and holding that Rule 414's incorporation of conduct prohibited in a federal statute does not incorporate that statute's interstate-commerce element because "the interstate character of a defendant's prior crimes has no bearing on the evidence's probative value"); *United States v. Shaw*, No. 22-CR-00105-BLF-1, 2023 WL 2815360, at *7 (N.D. Cal. Apr. 5, 2023) (analyzing legislative history of Rules 413-415 and holding that "the Court should look at the type of conduct at issue, as opposed to its location"); Advisory Note, *Report of the Judicial Conference on the Admission of Character Evidence in Certain Sexual Misconduct Cases*, 159 F.R.D. 51, 57 (Feb. 9, 1995) (proposing amendments to Rules 413-415, including to clarify "with no change in meaning" that "[e]vidence offered [of another sexual assault] must relate to a form of conduct proscribed by ... chapter 109A ... of title 18, United States Code, regardless of whether the actor was subject to federal jurisdiction").

In an analogous context, in *Torres v. Lynch*, the Supreme Court held that a New York state arson law was an "aggravated felony" under the Immigration and Nationality Act because it was an offense "described in" a federal arson statute, even though it lacked the federal statute's jurisdictional hook. 578 U.S. 452, 460, 473, 136 S.Ct. 1619, 194 L.Ed.2d 737 (2016). The Court reasoned that state legislatures are "not limited to Congress's enumerated powers" and therefore would have "no reason to tie their substantive offenses to those grants of authority." *Id.* at 458, 136 S.Ct. 1619; *see also id*. at 457, 136 S.Ct. 1619 (explaining that most federal criminal statutes include "substantive elements," which "primarily define[ ] the behavior that the statute calls a 'violation' of federal law," and a "jurisdictional element," which "ties the substantive offense ... to one of Congress's constitutional powers"). ***166** Rules 413-415 do not contain a "jurisdictional hook," and the drafters of the rules would not have been concerned with the lack of police power or any jurisdictional requirement because the Federal Rules of Evidence, unlike the federal criminal code, do not authorize federal punishment.

Accordingly, we give Rule 413 a common-sense reading that is consistent with the structure and purpose of Rules 413-415. We conclude that Rule 413(d)(1) applies to *conduct* that fits within chapter 109A -- such as aggravated sexual abuse, sexual abuse, sexual abuse of a minor, or abusive sexual contact -- without regard to whether chapter 109A's jurisdictional element is met. Therefore, the Stoynoff testimony was admissible under Rule 413(d)(5) as evidence of an attempt to engage in the type of conduct covered by Rule 413(d)(1).

Our holding that Ms. Stoynoff's testimony was properly admitted is further supported by Ms. Leeds's testimony and the *Access Hollywood* tape and the fact that the sufficiency standard for admitting the evidence under Rule 415 is lower than what would be required to sustain a conviction. Accordingly, the district court did not abuse its discretion in admitting the Stoynoff testimony. [18]

c. *The* Access Hollywood *Tape*

Mr. Trump's final challenge to the district court's admission of other act evidence centers on a 2005 recording of a conversation among Mr. Trump, Billy Bush, and others as they arrived for the filming of a television show. This recording, known as the *Access Hollywood* tape, aired nationally during the 2016 presidential election. The tape, just under two minutes long, was played twice for the jury. In the recording, Mr. Trump states that he "moved on" a woman

named Nancy "like a bitch" and "did try and fuck her." App'x at 2883. As he described the encounter:

> I moved on her actually. You know she was down on Palm Beach. I moved on her, and I failed. I'll admit it. I did try and fuck her. She was married. ... I moved on her very heavily in fact I took her out furniture shopping. She wanted to get some furniture. I said I'll show you where they have some nice furniture. I moved on her like a bitch, but I couldn't get there. And she was married. Then all-of-a-sudden I see her, she's now got the big phony tits and everything. She's totally changed her look.

Id. He also stated, "You know I'm automatically attracted to beautiful -- I just ***167** start kissing them. It's like a magnet. Just kiss. I don't even wait. And when you're a star, they let you do it. You can do anything. ... Grab them by the pussy. You can do anything." *Id*.

During his October 2022 deposition, Mr. Trump was questioned about his statements in the tape. A portion of that testimony was played to the jury:

> Q. And you say -- and again, this has become very famous -- in this video, 'I just start kissing them. It's like a magnet. Just kiss. I don't even wait. And when you're a star, they let you do it. You can do anything, grab them by the pussy. You can do anything.' That's what you said; correct?
>
> A. Well, historically, that's true with stars.
>
> Q. True with stars that they can grab women by the pussy?
>
> A. Well, that's what -- if you look over the last million years, I guess that's been largely true. Not always, but largely true. Unfortunately or fortunately.
>
> Q. And you consider yourself to be a star?
>
> A. I think you can say that, yeah.

Id. at 2973.

The district court concluded that the recording was admissible as evidence of a prior sexual assault because it satisfied the requirements of Rule 413(d)(2) as well as (d)(5). Thus, the district court ruled that a "jury reasonably could find, even from the *Access Hollywood* tape alone, that Mr. Trump admitted in the *Access Hollywood* tape that he in fact has had contact with women's genitalia in the past without their consent, or that he has attempted to do so." *Carroll*, 660 F. Supp. 3d at 203. In its post-trial decision denying Mr. Trump's motion for a new trial, however, the district court concluded that at trial "it became clear that reliance on Rule 415 was unnecessary because the video was offered for a purpose other than to show the defendant's propensity to commit sexual assault." *Carroll*, 683 F. Supp. 3d at 302, 313 n.20. Instead, the court concluded, the recording "could have been regarded by the jury as a sort of personal confession as to his behavior." *Id.* at 326.

The district court concluded that the recording was relevant because it "has the tendency to make [the] fact [of whether [Mr. Trump] sexually assaulted Ms. Carroll] more or less probable than it would be without the evidence because one of the women he referred to in the video could have been Ms. Carroll." *Id.* at 313 n.20 (internal quotation marks omitted).

We are not fully persuaded by the district court's second basis for admitting the recording -- that the tape captured a "confession." *Id.* at 326. But the first rationale adopted by the district court -- that the recording was evidence of one or more prior sexual assaults and therefore admissible under Rules 413 and 415 -- provided a proper basis for the district court's exercise of its broad discretion. As discussed above, we may reverse the district court's ruling only if we find it to have been "arbitrary and irrational." *Restivo v. Hessemann*, 846 F.3d 547, 573 (2d Cir. 2017) (quoting *United States v. Coppola*, 671 F.3d 220, 244 (2d Cir. 2012)).

Applying this highly deferential standard of review, we conclude that the district court did not abuse its discretion in admitting the recording pursuant to Rules 413(d)(2), 413(d)(5), and 415. In the recording, Mr. Trump says, "I just start kissing them," "I don't even wait," and "You can do anything. ... Grab them by the pussy." App'x at 2883. The jury could have reasonably concluded from those statements that, in the past, Mr. Trump had kissed women without their consent and then proceeded to touch their genitalia. While it is true, as ***168** Mr. Trump argues, that he also said, "[T]hey let you do it," the district court correctly observed that "[i]t simply is not the Court's function in ruling on the

admissibility of this evidence to decide what Mr. Trump meant or how to interpret his statements." *Carroll*, 660 F. Supp. 3d at 203. Rather, the court's duty was simply to decide whether a jury could reasonably find by a preponderance of the evidence that Mr. Trump committed an act of sexual assault (as defined under Rule 413). If it could so find, the court had the discretion to admit the evidence.

We also conclude that the *Access Hollywood* tape was admissible pursuant to Rule 404(b) as evidence of a pattern, or *modus operandi*, that was relevant to prove that the alleged sexual assault actually occurred (the *actus reus*). [19] *See* Leonard, *supra*, § 13.1 (recognizing that evidence of *modus operandi* may be admissible for a variety of non-propensity purposes, including "to demonstrate that the act at issue actually was committed").

The existence of a pattern, or a "recurring *modus operandi*," can be proven by evidence of "characteristics ... sufficiently idiosyncratic to permit a fair inference of a pattern's existence." *United States v. Sliker,* 751 F.2d 477, 487 (2d Cir. 1984); *see also Ismail v. Cohen*, 706 F. Supp. 243, 253 (S.D.N.Y. 1989) (admitting evidence under Rule 404(b) to show a "pattern of misconduct" involving defendant "applying handcuffs too tightly, falsely claiming injury from the citizen to cover up his own inappropriate use of physical force, and filing false charges for the same purpose"), *aff'd*, 899 F.2d 183, 188-89 (2d Cir. 1990) (no error in admitting other act evidence under Rule 404(b) for "pattern" purposes); *United States v. Carlton*, 534 F.3d 97, 101-02 (2d Cir. 2008) (holding that evidence of similarities between defendant's three prior bank robberies and the charged bank robbery -- "such as location, the takeover style of the robberies, or use of a getaway car" -- established "the existence of a pattern"). The similarities between the past acts and current allegations "need not be complete." *Sliker,* 751 F.2d at 487. It is enough for admissibility purposes that the acts be sufficiently similar as to "earmark them as the handiwork of the accused." *Id*. (quoting 1 McCormick, Evidence § 190, at 559 (3d ed. 1984)).

Courts have routinely admitted evidence of a pattern or *modus operandi* in sexual assault cases where, as here, the defendant is alleged to have engaged in a distinctive pattern of conduct related to non-consensual sexual contact. *See, e.g.*, *Roe v. Howard*, 917 F.3d 229, 245-46 (4th Cir. 2019) (no error in the admission of evidence of a pattern of prior sexual abuse under Rule 404(b) where the prior victim's testimony mirrored the plaintiff's allegations); *Montanez v. City of Syracuse*, No. 16-cv-00550, 2019 WL 4328872, at *4-7 (N.D.N.Y. Sept. 12, 2019) (admitting evidence of a prior sexual assault under Rule 404(b) as relevant to show, *inter alia*, a pattern because the previous victim and the plaintiff both alleged that the defendant, a law enforcement officer, "exposed himself to them while on duty, responding to calls at their residences, and intimidated them into performing oral sex"); Leonard, *supra*, § 13.3 (explaining that evidence of *modus operandi* may be relevant and admissible under Rule 404(b) in "[s]exual assault and ***169** child molestation cases" where the "crimes are committed in the presence of fewer people and leave fewer traces").

Evidence of a pattern may also be relevant for the non-propensity purpose of corroborating witness testimony. *United States v. Everett*, 825 F.2d 658, 660-61 (2d Cir. 1987) ("Under Rule 404(b) evidence of 'other crimes' has been consistently held admissible to corroborate crucial prosecution testimony" so long as "corroboration is direct and the matter corroborated is significant.") (internal quotation marks omitted); *United States v. Williams*, 577 F.2d 188, 192 (2d Cir. 1978) (noting that evidence of other acts may be admissible under Rule 404(b) "even if the trial court finds that such evidence is relevant only for corroboration purposes, provided that the corroboration is direct and the matter corroborated is significant"); *see also United States v. Cadet*, 664 F.3d 27, 32 (2d Cir. 2011) (listing "corroboration of witnesses" as one of the acceptable "non-propensity purposes" for admitting other act evidence under Rule 404(b)); *United States v. Oskowitz*, 294 F. Supp. 2d 379, 382 (E.D.N.Y. 2003) ("[C]orroboration is also an acceptable purpose to admit prior act evidence."). [20] Its use in this fashion must be assessed as well under Rule 403, of course, for unfair prejudice, but in a proper case the district court may admit it.

We conclude that the *Access Hollywood* tape described conduct that was sufficiently similar in material respects to the conduct alleged by Ms. Carroll (and Ms. Leeds and Ms. Stoynoff) to show the existence of a pattern tending to prove the *actus reus*, and not mere propensity. Mr. Trump's statements in the tape, together with the testimony of Ms. Leeds and Ms. Stoynoff (detailed above), establish a repeated, idiosyncratic pattern of conduct consistent with what Ms. Carroll alleged. [21] In each of the three encounters, Mr. Trump engaged in an ordinary conversation with a woman he barely knew, then abruptly lunged at her in a semi-public place and proceeded to kiss and forcefully touch her without her consent. The acts are sufficiently similar to show a pattern or "recurring *modus operandi*." *Sliker,* 751 F.2d at

487. Moreover, the tape was "directly corroborative" of the testimony of Ms. Carroll, Ms. Leeds, and Ms. Stoynoff as to the pattern of behavior each allegedly experienced, and "the matter corroborated" was one of the most "significant" in the case -- whether the assault of Ms. Carroll actually occurred. *Everett*, 825 F.2d at 660-61 (noting that other act evidence admissible for corroborative purposes ***170** must involve corroboration that is "direct and the matter corroborated [must be] significant" (internal quotation marks omitted)). Therefore, the evidence of other conduct was relevant to show a pattern tending to directly corroborate witness testimony and to confirm that the alleged sexual assault actually occurred. [22] The *Access Hollywood* tape was therefore properly admitted.

d. *Rule 403*

Mr. Trump's final argument with respect to the other acts evidence rests on Rule 403. He contends that the district court abused its discretion in admitting the evidence because the risk of unfair prejudice substantially outweighed the evidence's probative value, which he characterizes as "extremely limited." Appellant's Br. at 35.

We find no abuse of discretion in the district court's assessment of the other acts evidence under Rule 403. The testimony of Ms. Leeds and Ms. Stoynoff and Mr. Trump's statements on the *Access Hollywood* tape were highly probative, and their probative value was not substantially outweighed by any unfair prejudice.

First, evidence admitted under Rule 415 is presumptively probative in a sexual assault case such as this, which centers on the parties' respective credibility. *See Schaffer*, 851 F.3d at 178 ("In passing Rule 413, Congress considered '[k]nowledge that the defendant has committed rapes on other occasions [to be] critical in assessing the relative plausibility of [sexual assault] claims and accurately deciding cases that would otherwise become unresolvable swearing matches.' " (alterations in original) (quoting *United States v. Enjady*, 134 F.3d 1427, 1431 (10th Cir. 1998))).

Second, for the reasons we discussed above with regard to the admissibility of the *Access Hollywood* tape under Rule 404(b), the conduct described by the other act evidence is sufficiently similar in material respects to be probative. True, Mr. Trump's alleged assault of Ms. Leeds occurred on an airplane, and thus differed from the assaults described by Ms. Carroll and Ms. Stoynoff, but Ms. Leeds's testimony was not so dissimilar as to substantially outweigh its strong probative value.

Mr. Trump argues that the amount of time since the alleged acts, particularly with respect to Ms. Leeds's testimony, reduces their probative value. But we apply Rules 413-415 in a manner that effectuates Congress's intent. *See, e.g.*, *Schaffer*, 851 F.3d at 178. As the district court observed, Congress intentionally did not restrict the timeframe within which the other sexual act must have occurred to be admissible under Rules 413-415. *Carroll*, 660 F. Supp. 3d at 208. One of the original sponsors of the legislation proposing Rules 413-415 explained that "evidence of other sex offenses by the defendant is often probative and properly admitted, *notwithstanding very substantial lapses of time in relation to the charged offense or offenses*." 140 Cong. Rec. 23603 (1994) (remarks of Rep. Molinari) (emphasis added). In consideration of this express intent, we conclude that the time lapse between the alleged acts does not negate the probative value of the evidence of those acts to the degree that would be required to find an abuse of discretion in admitting them for the jury's consideration. *Accord, e.g.*, ***171** *United States v. O'Connor*, 650 F.3d 839, 853-54 (2d Cir. 2011) (no abuse of discretion in admission of evidence of sexual acts that occurred 30 years earlier); *United States v. Davis*, 624 F.3d 508, 511-12 (2d Cir. 2010) (evidence of molestation conviction 19 years earlier was properly admitted); *United States v. Larson,* 112 F.3d 600, 604-05 (2d Cir. 1997) (evidence of sexual acts occurring up to 20 years earlier was properly admitted).

Finally, we also find that the other act evidence was not unfairly prejudicial, as the incidents in question were "no more sensational or disturbing" than the acts that Ms. Carroll alleged Mr. Trump to have committed against her. *United States v. Curley*, 639 F.3d 50, 59 (2d Cir. 2011) (internal quotation marks omitted). [23]

B. *Excluded Evidence*

Mr. Trump's second category of challenges to the judgment below is based on the district court's decision to exclude, rather than admit, certain evidence. Specifically, Mr. Trump argues that the district court unreasonably restricted his defense by precluding (1) evidence that some of Ms. Carroll's legal fees were being paid for by one of Mr. Trump's political opponents and (2) portions of a transcript made by Ms. Carroll of a 2020 interview between Ms. Carroll and Ms. Stoynoff

that, Mr. Trump argues, suggests that Ms. Carroll coached Ms. Stoynoff on her testimony. Mr. Trump also asserts that the district court erred in preventing him from cross-examining Ms. Carroll on three matters: her out-of-court claim that she possessed Mr. Trump's DNA; her decision not to file a police report; and her failure to seek surveillance video footage from Bergdorf Goodman. We address each challenge in turn.

1. *Litigation Funding*

The district court did not abuse its discretion in excluding evidence related to litigation funding. Mr. Trump contends that this evidence was "proof that a billionaire critic of President Trump had paid [Ms. Carroll's] legal fees, and that [Ms. Carroll] lied about the funding during her deposition." Appellant's Br. at 41. Mr. Trump thus sought to offer this evidence to attack Ms. Carroll's credibility, and also as evidence of bias and motive.

a. *Ms. Carroll's Credibility*

"Except for a criminal conviction under Rule 609, extrinsic evidence is not admissible to prove specific instances of a witness's conduct in order to attack or support the witness's character for truthfulness." Fed. R. Evid. 608(b). But the court "may, on cross-examination, allow [specific instances] to be inquired into if they are probative of [a witness's] character for truthfulness or untruthfulness." *Id*.

At Ms. Carroll's October 2022 deposition, when *Carroll I* (but not this case) was ***172** pending, in response to a question asking whether she was "presently paying [her] counsel's fees," Ms. Carroll responded that hers was "a contingency case" and said that no one else was paying her legal fees. App'x at 1188. On April 10, 2023, however, Ms. Carroll's counsel disclosed to Mr. Trump's attorneys Ms. Carroll's refreshed recollection "that at some point her counsel secured additional funding from a nonprofit organization to offset certain expenses and legal fees." *Id.* at 1191. In response, the district court permitted defense counsel limited discovery into the litigation funding, and Ms. Carroll's knowledge of it, while reserving judgment on the relevancy of evidence relating to the issue.

The facts established during the ensuing discovery confirmed that Ms. Carroll's case was taken on a contingency fee basis, and that, in September 2020, Ms. Carroll's counsel received outside funding from a nonprofit to help offset costs. There was no evidence to suggest that Ms. Carroll was personally involved in securing the funding, interacted with the funder, received an invoice showing the arrangement before or after her counsel received the outside funding, or had discussed the arrangement with anyone between learning of it in September 2020 and being deposed in October 2022.

Upon consideration of this evidence, the district court granted Ms. Carroll's motion to preclude evidence and argument about the litigation funding in the case. The district court concluded:

> In general, litigation funding is not relevant. Here I allowed very limited discovery against what seemed to me a remote but plausible argument that maybe something to do with litigation funding arguably was relevant to the credibility of one or two answers by this witness in her deposition. I gave the defense an additional deposition of the plaintiff, and I gave the defense limited document discovery.
>
> On the basis of all that, I have concluded that there is virtually nothing there as to credibility. And even if there were, the unfair prejudicial effect of going into the subject would very substantially outweigh any probative value whatsoever.

App'x at 1659. We perceive no abuse of discretion here.

First, district courts regularly exclude evidence of litigation financing under Rule 401, finding it "irrelevant to credibility" and that it "does not assist the factfinder in determining whether or not the witness is telling the truth." *Benitez v. Lopez*, No. 17-cv-3827, 2019 WL 1578167, at *1 (E.D.N.Y. Mar. 14, 2019); *see also id.* at *2 (reviewing cases and noting that "[n]o case" of which the court was aware supports the claimed proposition that "litigation financing documents are generally probative of a plaintiff's credibility"); *In re Valsartan N-Nitrosodimethylamine (NDMA) Contamination Prods. Liab. Litig.*, 405 F. Supp. 3d 612, 615 (D.N.J. 2019) (collecting cases); *cf. Kaplan v. S.A.C. Cap. Advisors, L.P.*, No. 12-cv-9350, 2015 WL 5730101, at *5 (S.D.N.Y. Sept. 10, 2015) (in class action context, denying defendants' request for production of documents relating to plaintiffs' litigation funding on ground that defendants failed to "show that the requested documents are relevant to any party's claim or defense").

Second, the district court did not abuse its discretion in precluding cross-examination on this point because, as the district court found, Ms. Carroll's prior statement on the

litigation funding was not sufficiently probative of her credibility. Ms. Carroll plausibly represented that she had forgotten about the limited outside funding counsel obtained in September 2020 when this question was first posed to her in 2022, and the additional discovery ***173** did not indicate otherwise. Rather, it showed that Ms. Carroll simply was not involved in the matter of who was or was not funding her litigation costs. Ms. Carroll testified that, after her counsel informed her in September 2020 that they had received some outside funding, she did not speak with her counsel about this topic again until the spring of 2023 and did not even know the funder's political position or why they were partially funding her lawsuit. Therefore, by the time of her deposition in October 2022, Ms. Carroll had not spoken with her counsel about the matter of outside funding for over two years. It was not an abuse of the district court's discretion to conclude that the available litigation-funding evidence would have little probative value compared to its potential for unfair prejudice.

b. *Bias and Motive*

For similar reasons, we conclude that extrinsic evidence of the litigation funding had minimal, if any, probative value on the issue of Ms. Carroll's bias and motive. [24]

Extrinsic evidence may be introduced to prove a witness's bias. *United States v. Harvey*, 547 F.2d 720, 722 (2d Cir. 1976) ("[B]ias of a witness is not a collateral issue and extrinsic evidence is admissible to prove that a witness has a motive to testify falsely."). The admissibility of evidence for this purpose depends on whether it is "sufficiently probative of [the witness's asserted bias] to warrant its admission into evidence." *United States v. Abel*, 469 U.S. 45, 49, 105 S.Ct. 465, 83 L.Ed.2d 450 (1984).

To the extent Mr. Trump argues that the acceptance of outside funding goes toward Ms. Carroll's motive in lodging these allegations at Mr. Trump, the discovery also confirmed that Ms. Carroll publicly accused Mr. Trump of sexual assault over a year before the outside litigation funding was secured. Moreover, whether the outside funder was politically opposed to Mr. Trump was of little probative value because Ms. Carroll herself frankly admitted her political opposition to Mr. Trump, and her key witnesses testified to their opposition as well. *See, e.g.*, App'x at 1653 (Ms. Carroll acknowledging she is "a registered Democrat"); *id.* at 2120, 2123 (Ms. Leeds acknowledging she is a Democrat and "passionate about politics"); *id.* at 2054 (Ms. Birnbach acknowledging she is a Democrat and donated to Hillary Clinton); *id.* at 2411 (Ms. Martin acknowledging she is a Democrat and donated to Clinton). On multiple occasions, defense counsel was able to bring out the political opposition and distaste for Mr. Trump held by Ms. Carroll and her witnesses. *See United States v. James*, 609 F.2d 36, 47-48 (2d Cir. 1979) (finding reversal not warranted where defendant was given full opportunity to explore witness's apparent bias). [25]

***174** In light of the minimal probative value of the evidence, we conclude that the district court did not abuse its discretion in excluding it under Rule 403.

2. *The Stoynoff Transcript*

During trial, Mr. Trump moved to admit a redacted version of a transcript made by Ms. Carroll of a conversation between Ms. Carroll and Ms. Stoynoff to show Ms. Carroll's alleged "effort to influence Ms. Stoynoff's testimony." App'x at 1900. The court devoted over thirty minutes of a sidebar conversation to "trying to figure out what it is [defense counsel was] trying to put in[to evidence]." App'x at 1907; *see also id.* at 1912. [26] The district court called defense counsel's rendition of his proposed presentation to the jury of the redacted transcript "tremendously confusing," *id.* at 1903, and commented that defense counsel did not have the slides of the redacted transcript "figured out" or "put together," *id.* at 1907. At the end of this lengthy conversation, the district court denied the motion to receive the proposed document into evidence, finding that Ms. Stoynoff's statements in the transcript constituted hearsay, and that the proposed document's use at trial would be confusing and unnecessarily time-consuming. The court requested that defense counsel determine how to elicit the information "[i]n a way that will not be confusing and take three times as much time." *Id.* at 1913.

The solution that the court accepted, and that Mr. Trump now challenges as insufficient, was to exclude the redacted transcript from presentation on direct examination but to permit defense counsel to cross-examine Ms. Carroll about the interview and to use the transcript to refresh and impeach, if necessary. On cross-examination, defense counsel did in fact confront Ms. Carroll with language from the transcript, reading portions of it into the record. Defense counsel did not seek to question Ms. Stoynoff about the transcript.

Mr. Trump argues that the district court's decision to preclude the redacted Stoynoff transcript itself was erroneous: he submits that Ms. Carroll's statements, as they were embodied in the redacted transcript, were admissible for their truth as a party admission under Federal Rule of Evidence 801(d)(2)(A). Mr. Trump also argues that the transcript itself was admissible as extrinsic evidence of motive and bias.

We agree with Mr. Trump that, contrary to Ms. Carroll's argument, the Stoynoff transcript did not contain inadmissible hearsay: Ms. Carroll's statements were party admissions under Rule 801(d)(2)(A), and Ms. Stoynoff's responses were being offered to place Ms. Carroll's statements into context and were not being offered for their truth. *See United States v. Song*, 436 F.3d 137, 139 (2d Cir. 2006) (finding that it was error to exclude testimony not offered for the truth of the matters asserted, "but rather[ ] to demonstrate the motivation behind [a party's] actions"); ***175** *United States v. Ebens*, 800 F.2d 1422, 1430-32 (6th Cir. 1986) (holding that trial court erred in not admitting recording of witnesses being prepared, where tapes were not offered for truth of statements contained therein, but to show, *inter alia*, that witnesses were being coached), *abrogated in other respects by Huddleston v. United States*, 485 U.S. 681, 108 S.Ct. 1496, 99 L.Ed.2d 771 (1988). The transcript was also arguably relevant as extrinsic evidence of Ms. Carroll's bias. *See James*, 609 F.2d at 46; *Harvey*, 547 F.2d at 722.

But the district court did not err in refusing to admit the proposed redacted version of the transcript into evidence. We accord great deference to a district court "in determining whether evidence is admissible, and in controlling the mode and order of its presentation to promote the effective ascertainment of the truth." *SR Int'l Bus. Ins. Co. v. World Trade Ctr. Props., LLC*, 467 F.3d 107, 119 (2d Cir. 2006) (internal quotation marks omitted). As discussed above, a district court does not abuse its discretion in making an evidentiary ruling unless "the ruling was arbitrary and irrational." *Restivo*, 846 F.3d at 573 (quoting *Coppola*, 671 F.3d at 244). The district court's decision to exclude the Stoynoff transcript as prepared by counsel was far from arbitrary or irrational.

The district court's sidebar discussion with counsel illuminates that defense counsel sought to use the transcript in ways that risked confusion, undue delay, and wasted time on cumulative evidence -- considerations that the district court was permitted to weigh, pursuant to Federal Rule of Evidence 403, when deciding whether to admit or exclude the evidence. Defense counsel provided no explanation as to how the transcript itself would have added anything of significance, and the transcript's admission would have been largely cumulative of the excerpts that were read verbatim into the record. *See Old Chief v. United States*, 519 U.S. 172, 184-85, 117 S.Ct. 644, 136 L.Ed.2d 574 (1997) ("[W]hen Rule 403 confers discretion by providing that evidence 'may' be excluded, the discretionary judgment may be informed not only by assessing an evidentiary item's twin tendencies, but by placing the result of that assessment alongside similar assessments of evidentiary alternatives."). A trial judge has discretion to exclude cumulative proof of bias, including documentary evidence, when the witness admits to the "incidents from which any alleged bias ... arose." *United States v. Weiss*, 930 F.2d 185, 199 (2d Cir. 1991). Here, the district court permitted defense counsel to cross-examine Ms. Carroll using language drawn verbatim from the transcript, and Ms. Carroll admitted to all the relevant information. Moreover, the district court correctly instructed the jury to consider Ms. Stoynoff's statements not for their truth, but for "the fact that they were said to Ms. Carroll because they shed light on what Ms. Carroll did and why she did it." App'x at 1920. Accordingly, we conclude that the district court acted well within its discretion in excluding the Stoynoff transcript.

3. *DNA Evidence*

Mr. Trump next argues that the district court erred when it "precluded cross-examination of [Ms. Carroll] regarding her false, public claim that she possessed President Trump's DNA" on the dress she was wearing the day of the 1996 assault. Appellant's Br. at 48. In a written opinion issued pretrial, the district court concluded that although Ms. Carroll's statements regarding DNA evidence were arguably relevant to Ms. Carroll's credibility, their probative value was significantly outweighed by the reasons for preclusion enumerated in Rule 403, including "unfair ***176** prejudice, confusing the issues, misleading the jury, undue delay, [and] wasting time." *Carroll v. Trump*, No. 22-cv-10016 (LAK), 2023 WL 2652636, at *7 (S.D.N.Y. Mar. 27, 2023). We see no abuse of discretion here.

In a series of tweets on her public Twitter page in 2020 and 2021, Ms. Carroll claimed that she still had the dress she was wearing when Mr. Trump assaulted her, and she believed the dress had Mr. Trump's DNA on it. [27] She had had a DNA test performed on the dress, and the test showed, she said, that the dress had male DNA on it. *See* App'x at 599-601. At the outset

of *Carroll I*, Ms. Carroll had requested a DNA sample from Mr. Trump for testing, seeking to confirm her belief that it was his DNA, but Mr. Trump had refused to provide a sample for over three years and did not offer to provide a sample until the eve of trial in *Carroll II*. *See generally Carroll v. Trump*, No. 22-cv-10016 (LAK), 2023 WL 2006312, at *3-6 (S.D.N.Y. Feb. 15, 2023). The district court did not abuse its discretion in precluding cross-examination of Ms. Carroll on this subject.

First, the district court determined that the probative value of this line of questioning was low, as there was no credible evidence that Ms. Carroll lied about believing that Mr. Trump's DNA was on the dress. She was simply never able to confirm or negate the basis for her belief because she was never able to obtain a sample of Mr. Trump's DNA to compare to the DNA on the dress.

Second, the district court also recognized that cross-examination of Ms. Carroll on this basis would have opened the door to questions about why she never conducted a DNA test with Mr. Trump's sample, whether she had tried to get a DNA sample from Mr. Trump, and why she was unable to do so. Cross-examination in this area also could have required expert testimony on DNA testing. The parties indicated to the district court that if DNA became an issue, they would seek to reopen discovery, adduce expert testimony, and engage in a new round of motions *in limine* related to this topic.

We conclude that the district court did not abuse its discretion in determining that allowing further inquiry into this area created a substantial danger of unfair prejudice, confusion, and unnecessary delay. That danger substantially outweighed any possible probative value, especially considering that the pretrial discovery period had closed by the time Mr. Trump offered to provide a DNA sample, and both parties had had ample time to develop DNA as an issue, yet both had failed to do so. Permitting cross-examination on this issue would have created a "trial within a trial" about why Ms. Carroll did not have Mr. Trump's DNA sample. *See, e.g.*, *Ricketts v. City of Hartford*, 74 F.3d 1397, 1414 (2d Cir. 1996) (no abuse of discretion "in determining that a trial within a trial ... would have been more confusing than helpfully probative"); *United States v. Aboumoussallem*, 726 F.2d 906, 912-13 (2d Cir. 1984) (upholding ***177** exclusion of evidence under Rule 403 where confusion and delay caused by trial within a trial would substantially outweigh the evidence's probative value).

4. *Failure to File Police Report*

Mr. Trump also contends that the district court erred in precluding the following question to Ms. Carroll: "How would you bringing criminal charges be disrespectful to some people at the border?" App'x at 1840. The district court stated: "Correct me if I'm wrong, counsel, but I believe in the State of New York private individuals can't bring criminal charges," and explained, "We have been up and down the mountain on the question of whether she went to the police, so let's move on." *Id.*

Mr. Trump argues that he should have been permitted to pursue this line of questioning to explore further her decision not to use formal options for reporting her allegations. Mr. Trump also argues that the district court's response improperly suggested that Ms. Carroll was powerless to file a report.

The district court did not abuse its discretion in limiting this line of questioning or in making these brief comments. Mr. Trump's arguments on this point rely on a mischaracterization of the record. The district court permitted extensive questioning on cross-examination of Ms. Carroll regarding her decision not to go to the police, and the court allowed the introduction of extrinsic evidence on this very point. By the time Mr. Trump's counsel reached this question, Ms. Carroll had already responded to at least ten questions regarding her decision not to file a police report. The federal rules instruct the district court to "exercise reasonable control over the mode and order of examining witnesses and presenting evidence so as to ... make those procedures effective for determining the truth [and] avoid wasting time." Fed. R. Evid. 611(a). The district court was well within its discretion to bar further cumulative questioning.

5. *Bergdorf Goodman Security Footage*

Finally, the district court did not abuse its discretion when it denied Mr. Trump's counsel the opportunity to ask Ms. Carroll whether she went back to Bergdorf Goodman the "next day to ... ask for the video camera footage." App'x at 1842.

It is well established in our circuit that "a question (which assumes a fact) may become improper on cross-examination, because it may by implication put into the mouth of an unwilling witness, a statement which he never intended to make, and thus incorrectly attribute to him testimony which is

not his." *United States v. DeFillipo*, 590 F.2d 1228, 1239-40 (2d Cir. 1979) (quoting 3 Wigmore, Evidence § 780, at 171 (Chadbourn ed., rev. 1970)).

Right before this question was asked and objected to, Ms. Carroll had testified that she had "never ... been able to verify if there were cameras in the dressing room or in the lingerie department." App'x at 1841. And not one of the witnesses who testified about the location of cameras within the store at the time in question had stated that there were cameras in either of these locations. The former store manager at Bergdorf Goodman, Cheryl Beall, testified that she thought that, at the time, there were cameras at the main entrances and exits and "in fine jewelry" but not around the escalators or in the lingerie department. *Id.* at 1557-58. Likewise, the former Senior Vice President of Administration at Bergdorf Goodman, Robert Salerno, testified that he thought there were only a few cameras in the store in the mid-1990's -- at the employee entrance, at the loading dock, and maybe in ***178** furs, and in fine jewelry. Thus, by the time this question was asked, defense counsel had elicited no proof that video cameras were installed in the specific locations of the store where the incident occurred. Accordingly, the district court correctly determined that defense counsel's question to Ms. Carroll assumed a fact not in evidence. Moreover, notwithstanding the absence of evidence of cameras in the locations in question, Mr. Trump's counsel still emphasized this point during his closing argument. *Id.* at 2681 ("[S]he even told you she never even went back to think about looking for surveillance video at Bergdorf Goodman which would have proven her case. She didn't think about it because it never happened.").

C. ***No New Trial Is Warranted***

Finally, Mr. Trump asserts that he is entitled to a new trial, arguing that the cumulative effect of the claimed errors affected his substantial rights. "[A]n erroneous evidentiary ruling warrants a new trial only when 'a substantial right of a party is affected,' as when 'a jury's judgment would be swayed in a material fashion by the error.' " *Lore*, 670 F.3d at 155 (quoting *Arlio*, 474 F.3d at 51). "We measure prejudice by assessing error in light of the record as a whole." *Phillips v. Bowen*, 278 F.3d 103, 111 (2d Cir. 2002) (citation omitted). And, even assuming evidentiary error, we will not grant a new trial if we find that the error was "harmless." *Cameron*, 598 F.3d at 61. We will deem an evidentiary error harmless if we conclude that the proof at issue was "unimportant in relation to everything else the jury considered on the issue in question, as revealed in the record." *Yates v. Evatt,* 500 U.S. 391, 403, 111 S.Ct. 1884, 114 L.Ed.2d 432 (1991).

As we have discussed, the district court did not abuse its discretion in making any of the challenged evidentiary rulings. The jury made its assessment of the facts and claims on a properly developed record. Even assuming *arguendo* that the district court erred in some of these evidentiary rulings -- a proposition that we have rejected -- taking the record as a whole and considering the strength of Ms. Carroll's case, we are not persuaded that any claimed error or combination of errors in the district court's evidentiary rulings affected Mr. Trump's substantial rights. *Lore*, 670 F.3d at 155.

CONCLUSION

For the reasons set forth above, the judgment of the district court is AFFIRMED.

All Citations

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Footnotes

1 Ms. Carroll also testified that Mr. Trump inserted his penis into her vagina; the jury, however, found that she did not prove this part of her claim by a preponderance of the evidence.

2 Mr. Trump issued a public statement on June 21, 2019. It read in part:

> I've never met this person in my life. She is trying to sell a new book -- that should indicate her motivation. It should be sold in the fiction section. Shame on those who make up false stories of assault to try to

> get publicity for themselves, or sell a book, or carry out a political agenda -- like Julie Swetnick who falsely accused Justice Brett Kavanaugh. It's just as bad for people to believe it, particularly when there is zero evidence. Worse still for a dying publication to try to prop itself up by peddling fake news -- it's an epidemic. ... It is a disgrace and people should pay dearly for such false accusations.

App'x at 2839. Then-President Trump publicly denied the allegations two more times -- once to a reporter at the White House, and again in an interview with *The Hill*. In his interview with *The Hill*, he stated: "I'll say it with great respect: Number one, she's not my type. Number two, it never happened. It never happened, OK?" App'x at 2854. The statements Mr. Trump made while still President are the subject of the second trial, which is discussed *infra*.

3 *See supra* n.1. The jury also found that Ms. Carroll had not shown that Mr. Trump "raped" her. Jury Verdict Form, *Carroll II*, Dkt. 174.

4 *Carroll I* was not tried until January 16, 2024, that is, after the trial of *Carroll II* was completed. *Carroll I* (January 16, 2024 Minute Entry). In *Carroll I*, the jury found Mr. Trump liable for earlier instances of defamation and awarded Ms. Carroll $83 million in compensatory and punitive damages. Judgment, *Carroll I*, Dkt. 285 (Feb. 8, 2024).

5 Some have questioned whether allowing propensity evidence in sexual assault cases "could diminish significantly the protections that have safeguarded persons accused in criminal cases and parties in civil cases against undue prejudice." *Schaffer*, 851 F.3d at 180 & n.79 (quoting *Report of Judicial Conference on Admission of Character Evidence in Certain Sexual Misconduct Cases*, 159 F.R.D. 51, 53 (1995)). "[But t]he wisdom of an evidentiary rule permitting the use of propensity evidence in prosecutions for sexual assault is not 'the concern of the courts.' " *Id.* at 181. Absent some constitutional infirmity, "[d]eliberating the merits and demerits of Rule 413 is a matter for Congress alone." *Id.* (footnote omitted) (holding that Rule 413 does not violate due process).

6 *See* 140 Cong. Rec. 23,603 (1994) (statement of Rep. Molinari) ("The practical effect of the new rules is to put evidence of *uncharged offenses* in sexual assault and child molestation cases on the same footing as other types of relevant evidence that are not subject to a special exclusionary rule.") (emphasis added).

7 As the Third Circuit explained in *Johnson*:

> The principal sponsors of Rules 413-15, Representative Susan Molinari and Senator Robert Dole, declared ... that an address delivered to the Evidence section of the Association of American Law Schools by David J. Karp -- ... the drafter of Rules 413-15 -- was to serve as an "authoritative" part of the Rules' legislative history. 140 Cong. Rec. 23,602 (1994) (statement of Rep. Molinari); 140 Cong. Rec. 24,799 (1994) (statement of Sen. Dole). In the referenced speech, Mr. Karp stated clearly that "the standard of proof with respect to uncharged offenses under the new rules would be governed by the Supreme Court's decision in *Huddleston v. United States.*" [David J. Karp,] *Evidence of Propensity [and Probability in Sex Offense Cases and Other Cases]*, 70 Chi.-Kent L. Rev. [15, 19 (1994)].

Johnson, 283 F.3d at 153-54.

8 In her brief on appeal, Ms. Carroll notes that Mr. Trump failed to raise this argument in his briefings below, despite having ample opportunity to do so. Mr. Trump does not challenge this assertion, or make any further mention of his "based on" argument, in his reply brief.

9 "Under New York law a defamation plaintiff must establish five elements: (1) a written defamatory statement of and concerning the plaintiff, (2) publication to a third party, (3) fault, (4) falsity of the defamatory statement,

and (5) special damages or per se actionability." *Palin v. New York Times Co.*, 940 F.3d 804, 809 (2d Cir. 2019).

10 We do reach the argument, however, in our discussion below of the Stoynoff testimony.

11 The statute provided that an aircraft is "in flight ... from the moment when all external doors are closed following embarkation until the moment when one such door is opened for disembarkation." 49 U.S.C. § 1301(34) (1976); *see also* 49 U.S.C. § 1301(38) (Supp. III 1980).

12 Mr. Trump argues that because Ms. Leeds could not recall her embarkation point, the proof of jurisdiction is insufficient. But Ms. Leeds definitively recalled that the plane departed from one of only two possible locations -- either "Atlanta" or "Dallas" -- and had its final destination at LaGuardia Airport in New York. App'x at 2098, 2130. The alleged conduct therefore took place "within the United States" and thus within the "special aircraft jurisdiction of the United States" under either version of Ms. Leeds's testimony. *See* 49 U.S.C. § 1301(34) (1976); *see also* 49 U.S.C. § 1301(38) (Supp. III 1980).

13 The district court did not base its decision to admit the Leeds testimony on these specific statutes, *Carroll*, 660 F. Supp. 3d at 203-04, in part because Mr. Trump did not make these arguments below. But "[w]e are free to affirm on any ground that finds support in the record, even if it was not the ground upon which the trial court relied." *Beijing Neu Cloud Oriental Sys. Tech. Co. v. Int'l Bus. Machines Corp.*, 110 F.4th 106, 113 (2d Cir. 2024) (citation omitted).

14 Mr. Trump argues that Ms. Leeds's testimony was insufficient, as a factual matter, to support an attempt theory. The cases he cites, however, involve readily distinguishable conduct. In *Rapp v. Fowler*, for example, the witness had testified that the defendant put his hand on his knee and left it there for about 30 to 45 seconds. No. 20-cv-09586 (LAK), 2022 WL 5243030, at *2 (S.D.N.Y. Oct. 6, 2022). By contrast, Ms. Leeds testified that Mr. Trump put his hand up her skirt, wholly rejecting defense counsel's characterization that Mr. Trump had merely placed his hand on her knee. Similarly, in *United States v. Blue Bird*, 372 F.3d 989, 993 (8th Cir. 2004), no attempt was found where defendant had touched and kissed the victim but "desisted and withdrew when she said that she was not interested." *Accord United States v. Hayward*, 359 F.3d 631, 640 (3d Cir. 2004) (finding act of pushing a victim's head toward one's *clothed* genitals was ambiguous and not a substantial step toward contact between the mouth and genitals). Here, the jury could have reasonably found that Mr. Trump placed his hand underneath Ms. Leeds's clothing and did not withdraw it voluntarily.

15 "[P]ieces of evidence must be viewed not in isolation but in conjunction." *United States v. Carson*, 702 F.2d 351, 362 (2d Cir. 1983). Indeed, we have often observed that "bits and pieces" of evidence, taken together, can create a fuller picture -- such as a "mosaic" of intentional discrimination. *Vega v. Hempstead Union Free Sch. Dist.*, 801 F.3d 72, 86 (2d Cir. 2015); *see also Palin v. New York Times Co.*, 113 F.4th 245, 272 (2d Cir. 2024) ("When conducting this examination [under Rule 104(b)], 'the trial court must consider all evidence presented to the jury' because '[i]ndividual pieces of evidence, insufficient in themselves to prove a point, may in cumulation prove it.' " (quoting *Huddleston*, 485 U.S. at 690-91, 108 S.Ct. 1496)).

16 Chapter 109A is entitled "Sexual Abuse" and includes, *inter alia*, sections 2241 through 2244, each of which criminalizes conduct "in the special maritime and territorial jurisdiction of the United States or in a Federal prison" or certain other custodial facilities. 18 U.S.C. §§ 2241, 2242, 2243, 2244.

17 Rules 413-415 were introduced in materially identical form as part of the proposed, but not enacted, Comprehensive Violent Crime Control Act of 1991. *See* 137 Cong. Rec. 6003-04. When the Rules were re-introduced and passed as part of the Violent Crime Control and Law Enforcement Act of 1994, the section-by-section analysis of the Rules that accompanied the 1991 legislation, 137 Cong. Rec. 6030-34, was described by the Rules' original co-sponsors as a key part of the Rules' legislative history that "deserve[s] particular

attention." 140 Cong. Rec. 24,799 (statement of Sen. Dole); *see also* 140 Cong. Rec. 23,602 (statement of Rep. Molinari).

18 In allowing Ms. Stoynoff to testify, the district court also relied on Ms. Stoynoff's deposition, where she stated that Mr. Trump groped her without her consent. *See* App'x at 146 ("I consider that he lied about kissing and groping me without consent."). While Ms. Stoynoff did not ultimately use the word "grope" at trial, the district court did not abuse its discretion in relying on the deposition testimony in deciding to admit the evidence. As the district court reasoned in denying Mr. Trump's motion *in limine* to exclude Ms. Stoynoff's testimony, "the circumstances of the alleged encounter are relevant," including that Mr. Trump invited Ms. Stoynoff "to an unoccupied room and closed the door behind her," and then "he immediately, and without her consent, began kissing Ms. Stoynoff and pressed on as she resisted his advances" -- actions the court found to be "suggestive of a plan, formed before Mr. Trump invited Ms. Stoynoff to the unoccupied room and closed the door behind her, to take advantage of that privacy and to do so without regard to Ms. Stoynoff's wishes." *Carroll*, 660 F. Supp. 3d at 206. The court noted that the *Access Hollywood* tape and Ms. Leeds's testimony "are additional evidence that a jury would be entitled to consider in deciding whether to infer that the ultimate goal of Mr. Trump's alleged actions" was to attempt to sexually assault Ms. Stoynoff. *Id*. We further conclude, based on the above discussion, that Ms. Carroll elicited sufficient evidence for the jury to reasonably find by a preponderance of the evidence that Mr. Trump attempted to sexually assault Ms. Stoynoff.

19 To the extent that the district court's post-trial "confession" rationale for admitting the *Access Hollywood* tape -- that the tape "could have been regarded by the jury as a sort of personal confession as to his behavior," *Carroll*, 683 F. Supp. 3d at 326 -- is consistent with our above explanation that the tape was admissible under Rule 404(b) as evidence of a pattern of conduct, we identify no error.

20 In the related context of Rules 413-415, courts have also upheld the admissibility of evidence that is challenged as unfairly prejudicial where such evidence shows a pattern of behavior that corroborates witness testimony. *See United States v. Gaudet*, 933 F.3d 11, 18 (1st Cir. 2019) ("[The witness's] testimony was probative because it helped to establish the credibility of [the victim's] testimony" and "because the near identical account of abuse that she offered helped to corroborate [the victim's] allegations by illustrating that [the witness] had leveled nearly identical allegations against [the defendant] previously."); *United States v. Joubert*, 778 F.3d 247, 254-55 (1st Cir. 2015) ("[B]ecause [the defendant's] defense was that he did not commit the crimes against [the child victim], evidence bearing on [the child's] veracity was probative to determining whether [the defendant] indeed produced and possessed the illicit recording. The uncharged child molestation testimony was probative of [the child]'s veracity because it corroborated aspects of [the child]'s testimony, particularly the nature of the abuse and [the defendant's] modus operandi in approaching his victims.").

21 *Cf*. *United States v. Mohel*, 604 F.2d 748, 751 n.6 (2d Cir. 1979) ("The fact that the [other act] evidence is in the form of statements by the defendant himself does not change the applicable analysis.").

22 As our discussion makes clear, while *modus operandi* evidence is often relevant to identify the unknown perpetrator of a crime, "[it] is not in fact synonymous with 'identity.' " Leonard, *supra*, § 13.1. It can be -- and in this case it is -- relevant for other non-propensity purposes as well.

23 On appeal, Mr. Trump also offered brief challenges to the district court's admission of certain other evidence, including: (1) excerpts from two 2016 campaign videos in which Mr. Trump denied the allegations made by Ms. Leeds and Ms. Stoynoff; (2) additional testimony from Ms. Leeds, including, for example, regarding her reaction to statements made by Mr. Trump during the campaign; (3) additional testimony from Ms. Stoynoff, including, for example, her testimony regarding her belief that Mr. Trump engaged in this conduct with many women; and (4) evidence of certain other comments made by Mr. Trump. We discern no abuse of discretion in these rulings. Mr. Trump did not object to much of this additional evidence at trial, and he was able to

use some of the same testimony as impeachment material on cross-examination. Even assuming error in any of these rulings, Mr. Trump failed to carry his burden to show that his "substantial rights" were affected. *Tesser*, 370 F.3d at 319.

24 "Bias is a term used ... to describe the relationship between a party and a witness which might lead the witness to slant, unconsciously or otherwise, his testimony in favor of or against a party. Bias may be induced by a witness'[s] like, dislike, or fear of a party, or by the witness'[s] self-interest." *United States v. Abel*, 469 U.S. 45, 52, 105 S.Ct. 465, 83 L.Ed.2d 450 (1984).

25 Mr. Trump separately argues that the district court also "improperly restricted questioning and argument regarding [an attorney, George] Conway." Appellant's Br. at 43. Ms. Carroll testified at trial that about one month after she publicly accused Mr. Trump of sexually assaulting her, she attended a party where she met a lawyer named George Conway. Mr. Conway encouraged Ms. Carroll to seriously consider filing a lawsuit against Mr. Trump. The district court sustained an objection to portions of Mr. Trump's opening statement that concerned Mr. Conway on the ground that counsel was impermissibly arguing to the jury that Mr. Conway had recommended Ms. Carroll's counsel. Even if Mr. Conway's conversation with Ms. Carroll was somehow probative of bias, we find no error in the district court's ruling. Argument related to Ms. Carroll's choice of counsel had been ruled inadmissible pursuant to Ms. Carroll's unopposed motion *in limine*. *Carroll v. Trump*, No. 22-cv-10016 (LAK), 2023 WL 2652636, at *8 (S.D.N.Y. Mar. 27, 2023). Further, contrary to Mr. Trump's representation on appeal, defense counsel was permitted to meaningfully cross-examine Ms. Carroll about Mr. Conway. Ms. Carroll acknowledged that Mr. Conway had encouraged her to file the lawsuit, and defense counsel was able to argue these facts to the jury during summation.

26 The "transcript" document included much extraneous material. *See* App'x at 1371-415.

27 @ejeancarroll, Twitter (June 2, 2021, 12:10 PM), https://twitter.com/ejeancarroll/status/1400122740720480262 [https://perma.cc/W845-73S2] ("Didn't last as long as DNA on a dress."); @ejeancarroll, Twitter (Feb. 25, 2021, 12:49 PM), https://twitter.com/ejeancarroll/status/1364995845439901700 [https://perma.cc/MCQ7-ZTHD] ("Cyrus Vance, the Manhattan District Attorney, has Trump's taxes. Fani Willis, the Georgia Prosecutor, has Trump's phone call. Mary Trump has her grandfather's will. And I have the dress. Trump is basically in deep shit."); @ejeancarroll, Twitter (May 1, 2020, 3:16 PM), https://twitter.com/ejeancarroll/status/1256301599426785280 [https://perma.cc/PAR7-HPYM] ("I am STILL waiting for Trump to provide his DNA sample to be tested against the dress I wore when he attacked me.").

End of Document

EX-10.1 2 ex_168050.htm EXHIBIT 10.1

Exhibit 10.1

Litigation Funding Agreement

This Litigation Funding Agreement ("Agreement") is made and entered into as of December 27, 2019 (the "Effective Date") by and between LEGALIST FUND II, L.P., a Delaware limited partnership (the "Funder"), and DiaMedica Therapeutics Inc., a corporation organized under the laws of British Columbia, Canada and headquartered in Minnesota, United States of America (the "Plaintiff"). Each of the Funder and the Plaintiff is individually referred to as a "Party" hereunder and collectively, the "Parties" hereunder.

Recitals

A. The Plaintiff has filed a lawsuit against PRA Health Sciences, Inc. and Pharmaceutical Research Associates Group B.V. (collectively, the "Defendant") in an action styled: *DiaMedica Therapeutics Inc. v. PRA Health Sciences, Inc., et al.*, Case No. 1:18-cv-01318-MN, currently pending in the United States District Court for the District of Delaware (the "Action") in connection with the Claim(s) (as defined below) it has against the Defendant.

B. The Plaintiff is being advised on and/or represented in connection with the Claim(s) by Fisher Broyles LLP (the "Lead Counsel").

C. The Plaintiff and the Funder have agreed that the Funder will provide certain funding to facilitate the prosecution of the Claim(s) in exchange for certain payments if any recovery is awarded to the Plaintiff in connection with the Claim(s).

Agreement

The Plaintiff and the Funder, in consideration of the foregoing recitals, the mutual covenants, promises, and agreements hereinafter set forth, the mutual benefits to be gained by the performance thereof, and for other good and valuable consideration, the receipt and sufficiency of which is hereby acknowledged and accepted, intend to be legally bound by the terms and conditions of this Agreement.

1.0 Definitions

"Agreement" has the meaning set forth in the introductory paragraph.

"Budget" means the Lead Counsel's reasonable estimate of the funding required to pursue the Claim(s), which is attached hereto as Exhibit A and may be amended by the Parties from time to time in accordance with Section 9.8 of this Agreement.

"Claim(s)" means the claims and causes of action asserted by the Plaintiff in the Action, and in each and every Proceeding(s) (as defined below), as may be amended from time to time, arising out of or in connection with such claims and causes of action.

"Claim Proceeds" means any and all net proceeds, receivables, property, cash, and other consideration due to and/or received by, on behalf of, or in lieu of payment to, the Plaintiff arising out of or in connection with the Claim(s) as a result of any judgment, award, order, settlement arrangement, and/or compromise (including payment of any damages (whether treble, compensatory, punitive, or special), compensation, interest, restitution, recovery, judgment sum, arbitral award, settlement sum, compensation payment, costs, and interest on costs), whether in monetary or non-monetary form, whether actual or contingent, and before deduction of any taxes which the Plaintiff may be liable to pay in connection with such value due to and/or received by Plaintiff; but after deduction of recoupments or setoffs in respect of any claim or counterclaim asserted against Plaintiff by the Defendant; provided, however, that notwithstanding the foregoing, Claim Proceeds shall not include specific performance or any injunctive relief by the Defendant, including, without limitation, production of clinical records or performance of services.

"Committed Funds" means up to an aggregate of $1,000,000.00.

"Common Interest Material" means any discussion, evaluation, negotiation, or any other communication or exchange of information relating to the Claim(s) in any way, whether written or oral, between or among the Plaintiff, the Lead Counsel, the Funder, and/or the Funder's legal counsel, provided that such communication or exchange of information would be protected by attorney–client privilege between the Lead Counsel and the Plaintiff, the attorney work-product doctrine, or some other privilege or discovery protection if not disclosed to a third party lacking a common legal interest.

"Confidential Information" means the Common Interest Material and, to the extent not already covered as Common Interest Material, any communication or exchange of information relating to the Claim(s), including: (a) information, of any type, relevant to understanding the Claim(s); (b) the Lead Counsel's or the Funder's counsel's strategies, tactics, analyses, or expectations of the Parties to the Proceeding(s), regarding the Claim(s) or Claim Proceeds; and (c) any professional work product relating to the Claim(s) or the Claim Proceeds, whether prepared for the Plaintiff, the Lead Counsel, the Funder, or the Funder's counsel. Notwithstanding the foregoing, Confidential Information does not include information that (i) was or becomes generally available to the public other than by breach of this Agreement; (ii) was, as documented by the written records of the receiving Party, known by the receiving Party at the time of disclosure to it or was developed by the receiving Party or its representatives without using Confidential Information or information derived from it; or (iii) was disclosed to the receiving Party in good faith by a third party who has an independent right to such subject matter and information.

"Costs and Disbursements" means the legal fees, court costs, and other miscellaneous expenses specified in the Budget or approved by the Lead Counsel.

"Lead Counsel" has the meaning set forth in the recitals.

"Defendant" has the meaning set forth in the recitals.

"Effective Date" has the meaning set forth in the introductory paragraph.

"Funder" has the meaning set forth in the introductory paragraph.

"Funder Costs Amount" means the total of all Costs and Disbursements actually paid or otherwise funded by the Funder pursuant to this Agreement plus the reimbursement of $10,000.00 to the Funder for its diligence and underwriting costs, whether or not those Costs or Disbursements were reasonably incurred by the Plaintiff in accordance with this Agreement, or whether or not they were specified in the Budget.

"Funder Recovery Amount" means the greater of: [1,2]

(i) $1,000,000.00 if repayment occurs within nine (9) months of the Transfer Date, $2,000,000.00 if repayment occurs after nine (9) months from the Transfer Date but before trial has begun, or $3,000,000.00 thereafter; or

(ii) twenty percent (20%) of the Claim Proceeds.

"JAMS" has the meaning set forth in Section 9.5.

"Non-Monetary Claim Proceeds Fair Market Valuation" means the Plaintiff's good faith determination of the fair market value of any and all non-monetary Claim Proceeds constituting real or personal property other than cash; provided, however, that such Non-Monetary Claim Proceeds Fair Market Valuation shall not include specific performance by the Defendant or any injunctive relief against any Defendants, including without limitation, production of clinical records or performance of services.

[1] Note that in all cases, this is the premium amount paid in addition to the repayment of actual funds spent.

[2] In the event of a termination of this Agreement by either or both of the Parties, the percentage in subsection Funder Recovery Amount will be multiplied by the percentage of the Committed Funds actually paid by the Funder prior to termination.

"Plaintiff" has the meaning set forth in the introductory paragraph.

"Proceeding(s)" means each and every litigation or alternative dispute resolution proceeding arising out of or in connection with the Claim(s), including any settlement negotiation, arbitration, mediation or appeal, as well as any other proceedings which Funder and Plaintiff agree in writing shall be the subject of this Agreement. For the avoidance of doubt, Proceedings shall not include any proceedings governed by Section 9.5 of this Agreement.

"Obligations" means (a) the obligation of the Plaintiff to pay the Funder Costs Amount and Funder Recovery Amount to the Funder, (b) all other debts, liabilities, obligations, covenants and duties of the Plaintiff to the Funder now or hereafter existing, whether joint or several, direct or indirect, absolute or contingent, or due or to become due, arising under or in connection with this Agreement, or any of the transactions contemplated thereby and including any interest due thereon all as set forth in this Agreement; (c) all debts, liabilities, obligations, covenants and duties of the Plaintiff to pay or reimburse the Funder for all expenses, including reasonable out-of-pocket and documented attorneys' fees, incurred by the Funder in connection with the enforcement, attempted enforcement, or preservation of any rights or remedies under this Agreement, including all such costs and expenses incurred during any legal proceeding, including any proceeding under any applicable bankruptcy, insolvency or other similar debtor relief laws; and (d) all interest and fees on any of the foregoing, whether accruing prior to or after the commencement by or against Plaintiff of any proceeding under any applicable bankruptcy, insolvency, or other similar debtor relief laws naming Plaintiff as the debtor in such proceeding, regardless of whether such interest and fees are allowed claims in such proceeding.

"Transfer Date" means the date on which the Action is transferred to the U.S. District Court for the District of Minnesota.

2.0 Funding Terms

2.1 Agreement to Fund Plaintiff. In return for the Plaintiff's agreement to pay from any Claim Proceeds recovered the Funder Costs Amount and the Funder Recovery Amount to the Funder in accordance with the terms of this Agreement, the Funder agrees to pay reasonable Costs and Disbursements in accordance with the terms of this Agreement.

2.1.1 Transfer of Case or Denial of Motion. Plaintiff has filed a motion to transfer venue of the Claims from Delaware to Minnesota. The Funder's agreement to pay reasonable Costs and Disbursements is conditioned on the Claims being transferred to the U.S. District Court for the District of Minnesota. Plaintiff has an obligation to inform Funder when the motion is decided. The Funder shall promptly, no later than three (3) business days after receiving notice of the transfer, advance to the Plaintiff $200,000.00 to an account designated in writing by the Plaintiff to the Funder, which sum represents fees and costs previously paid by Plaintiff in the Action.

2.2 Reasonable Costs and Disbursements Only. Unless otherwise agreed by the Funder, the Funder will not pay and will not be liable under this Agreement for any unreasonable Costs and Disbursements, including without limitation, the following costs, disbursements, or liabilities that may be incurred by the Plaintiff:

2.2.1 costs and/or other sums incurred as a result of the Plaintiff's willful failure (on any one or more occasions) to cooperate with or to follow the advice of the Lead Counsel, subject to Section 6.4;

2.2.2. costs and/or other sums incurred as a result of any default by the Plaintiff under this Agreement after the expiration of any applicable grace or cure period hereunder;

2.2.3 any liability for payment of the Defendant's costs or the Plaintiff's liability for fines or penalties as set forth in a final non-appealable order or decision entered in the Action;

2.2.4 costs and/or other sums incurred as a result of any unreasonable failure by the Plaintiff or the Lead Counsel to comply with applicable law, an order or procedural rule of the applicable court during the Proceedings, or any discovery or other related obligations, in each instance, as set forth in a final non-appealable order or decision entered into in such Proceedings;

2.2.5 costs and/or other sums incurred as a result of any sanctions ordered against the Plaintiff or the Lead Counsel in the Proceedings;

2.2.6 costs and/or other sums incurred prior to the Effective Date (unless such costs are included in the Budget or in this Agreement) or after the term of this Agreement;

2.2.7 costs and/or other sums incurred over sixty (60) days prior to the date the invoice is submitted to the Funder, except as otherwise provided in Sections 2.2.1 and 2.2.6 above; or

2.2.8 any Costs or Disbursements in excess of the Committed Funds.

2.3 Payment Terms; Disputed Amounts. The Plaintiff shall instruct the Lead Counsel and any other service providers provided for in the Budget to address invoices relating to the work described in the Budget to the Plaintiff but mark such invoices payable by the Funder, and to deliver such invoices to the Plaintiff (with a copy delivered to the Funder simultaneously) for payment. After the Plaintiff approves such invoices and the Funder agrees that the Costs and Disbursements on an invoice are reasonable, the Funder shall promptly pay (without setoff, claims, defenses or any deduction) the applicable amount when due up to an aggregate amount not to exceed the Committed Funds. If the Funder, in its reasonable opinion, believes that some or all of the Costs and Disbursements on an invoice are unreasonable and are not required to be paid by the Funder pursuant to this Agreement, the Funder shall provide a written notice setting out the reasons for its belief to the Plaintiff (with a copy to the relevant billing party simultaneously) within twenty (20) days of receipt of the invoice. In the event the Funder provides such a notice, the Funder and the Plaintiff agree to work together with the relevant billing party to resolve the disputed amounts. Pending resolution of such disputed amounts, the Funder shall pay any Costs and Disbursements that are not subject to dispute. In the event that the Funder and Plaintiff are unable to resolve the disputed amounts within thirty (30) days, the Funder and the Plaintiff shall rely on the arbitration procedure set out in Section 9.5 for resolution. The Parties acknowledge and agree that the funding by the Funder to the Plaintiff shall be on a non-recourse basis except to the extent of the Funder's right to share in the Claim Proceeds as set forth in this Agreement.

2.4 Failure to Fund; Cessation of Funding. If the Funder fails to timely release and/or notifies the Plaintiff that it will cease to pay Costs and Disbursements in accordance with the terms of this Agreement, the Plaintiff shall thereafter exercise its reasonable best efforts to enter into alternative funding arrangements in connection with the Claim(s). Funder acknowledges and agrees that it will accept the subordination of its right or entitlement to the Funder Costs Amount or the Funder Recovery Amount to facilitate Plaintiff's ability to secure alternative funding arrangements.

2.5 Change to Lead Counsel Agreement. If Costs and Disbursements under this Agreement include fees for the Lead Counsel, the Plaintiff verifies that the Lead Counsel and the Plaintiff have modified their fee agreement for advice and/or representation in connection with the Claim(s) to convert 25 percent of the Lead Counsel's hourly rate to an alternative fee agreement, which does not affect the Funder's priority on the Funder Costs Amount or the Funder Recovery Amount.

3.0 Recovery Terms

3.1 Agreement to Pay Funder. The Funder Costs Amount and the Funder Recovery Amount shall become payable only in the event that the Plaintiff recovers Claim Proceeds and in all other circumstances shall be non-recourse. In return for the Funder's agreement to pay the Plaintiff's reasonable Costs and Disbursements incurred in accordance with the terms of this Agreement, the Plaintiff agrees to pay the Funder, upon recovery of Claim Proceeds, the Funder Costs Amount and the Funder Recovery Amount. The Plaintiff acknowledges and agrees that the Funder's entitlement to the Funder Costs Amount and the Funder Recovery Amount shall begin to accrue upon the Funder's payment of any portion of the Committed Funds and continue to accrue with subsequent payments by the Funder pursuant to this Agreement, whether or not the Funder provides the entirety of the Committed Funds but only for so long as this Agreement is not terminated by the Funder or by the Plaintiff as a result of the Funder's breach of this Agreement, in which event, Funder Costs Amount and Funder Recovery Amount will be proportionately reduced as noted above. If the Claim Proceeds are insufficient to pay in full both the Funder Costs Amount and the Funder Recovery Amount, then the Claim Proceeds shall be applied exclusively and entirely to paying these amounts to the Funder, after which no further sum shall be due and/or payable to the Funder by the Plaintiff or any other Person pursuant to this Agreement.

3.2 Payment of Claim Proceeds; Non-Monetary Claim Proceeds. The Plaintiff agrees that the Lead Counsel will hold any Claim Proceeds received by it or by the Lead Counsel on its behalf in trust for the Funder, on terms that shall entitle the Funder to receive such part of the Claim Proceeds as shall be equal to the total of the Funder Costs Amount and the Funder Recovery Amount to the extent of such Claim Proceeds. The Plaintiff shall use its good faith best efforts to release Claim Proceeds to the Funder to pay the Funder Costs Amount and the Funder Recovery Amount pursuant to this Agreement as promptly as possible. All Claim Proceeds received in monetary form shall be paid into the Lead Counsel's escrow account immediately upon receipt for further payment to the Funder. In the case of Claim Proceeds received in non-monetary form constituting real or personal property other than cash, as defined above, provided that monetary Claim Proceeds are inadequate to fund the Funder Costs and Funder Recovery Amounts, and unless otherwise agreed by the Funder and the Plaintiff in writing, the Plaintiff shall, as promptly as practicable, pay into the Lead Counsel's escrow account an amount equal to the Non-Monetary Claim Proceeds Fair Market Valuation and simultaneously provide to the Funder in writing (with a copy delivered to the Lead Counsel simultaneously) a statement of the details of the Non-Monetary Claim Proceeds Fair Market Valuation. If the Funder, in its reasonable opinion, disagrees with the Non-Monetary Claim Proceeds Fair Market Valuation, the Funder shall provide a written notice setting out the reasons for its belief to the Plaintiff (with a copy to the Lead Counsel simultaneously) within twenty (20) days of receipt of the Non-Monetary Claim Proceeds Fair Market Valuation statement. In the event the Funder provides such a notice, the Funder and the Plaintiff agree to work together to resolve the disputed fair market value determination of the non-monetary Claim Proceeds. In the event the Funder and the Plaintiff are unable to resolve the disputed fair market value determination of the non-monetary Claim Proceeds within thirty (30) days, the Funder and the Plaintiff shall rely on the arbitration procedure described in Section 9.5 for resolution. Notwithstanding anything to the contrary in this Agreement, no Claim Proceeds shall be released from the Lead Counsel's escrow account until such dispute is finally resolved in accordance with this Section 3.2.

3.3 Unexpected Delay. "Unexpected Delay" occurs when repayment has not occurred within three and one-half (3.5) years past the Transfer Date, and thereafter, the Funder shall receive interest on such unpaid amounts equal to 20% per annum commencing on the three and one-half year anniversary of the Transfer Date and which shall be added to the Funder Costs Amount and Funder Recovery Amount. Such interest will be calculated on an annual basis and will be added to the principal at the end of the prior year. End of year principal will include Funder Costs Amount and Funder Recovery Amounts due based on funding and recovery terms set forth above, plus additional interest accrued to date as provided in this Section 3.3.

4.0 Plaintiff's Representations and Warranties

The Plaintiff represents and warrants to the Funder as follows:

4.1 Full Disclosure. The Plaintiff and the Lead Counsel have provided the Funder with all material information relating to the Claim(s), as requested by the Funder, excluding information protected solely by the attorney–client privilege. To the Plaintiff's knowledge, all information the Plaintiff and the Lead Counsel have provided to the Funder is true and correct in all material respects.

4.2 No Impairment. Other than as already disclosed to the Funder in writing prior to the date hereof or as alleged by the Defendants in the Action, the Plaintiff has not taken any action (including executing documents) or failed to take any action to its knowledge that (a) would materially and adversely affect the Claim(s), or (b) would give any person or entity (other than the Funder and the Plaintiff) an interest in the Claim Proceeds.

4.3 Solvency. The Plaintiff has no bankruptcy proceedings outstanding and has not received any written notice of potential proceedings against it.

4.4 Authority. The Plaintiff is duly organized, validly existing, and in good standing under the laws of its jurisdiction of organization. The Plaintiff has the power and authority to execute and deliver this Agreement and to consummate the transactions contemplated hereby. The execution and delivery of this Agreement and the consummation of the transactions contemplated hereby have been duly authorized by all necessary corporate (or, if applicable, other entity) action on the part of the Plaintiff and no further corporate (or, if applicable, other entity) action is required on the part of the Plaintiff to authorize this Agreement and the transactions contemplated hereby. This Agreement has been duly executed and delivered by the Plaintiff and constitutes the valid and binding obligations of the Plaintiff, enforceable in accordance with its terms, subject to (a) laws of general application relating to bankruptcy, insolvency, and relief of debtors and (b) rules of law governing specific performance, injunctive relief, and other equitable remedies.

4.5 Common Interest. The Plaintiff has received the advice of the Lead Counsel, or of another duly qualified law firm or attorney, regarding the common interest doctrine in California.

5.0 Funder's Representations and Warranties

The Funder represents and warrants to the Plaintiff as follows:

5.1 Committed Funds. The Funder has, and will continue at all times during the term of this Agreement to have, sufficient funds available to fulfill its obligations under this Agreement.

5.2 No Conflicts. Other than as already disclosed to Plaintiff, the Funder has not, as of the Effective Date, (a) paid a referral fee to the Lead Counsel in connection with the Claim(s), the Plaintiff, or this Agreement; (b) entered into any transaction with the Lead Counsel that has or would make the Lead Counsel a part owner of the Funder; (c) contracted with any other party or potential party to the Claim(s); (d) engaged in negotiations with any other party or potential party to the Claim(s); or (e) entered into any relationship with the Lead Counsel that conflicts with the Plaintiff's interests regarding the Claim(s). The Funder does not have a duty, contractual obligation, or other requirement to monetize its interest in the Claim(s) within any particular time frame or which would require the Funder to cease funding the Claim(s). For the avoidance of doubt, the preceding sentence does not include a fiduciary duty that would require the Funder to cease funding the Claim(s) pursuant to Section 8.2.3 because of the Funder's assessment of the viability of the Claim(s). In addition, the Funder has not instituted any action, suit, or arbitration separate from the Claim(s) arising from the same facts, circumstances or law giving rise to the Claim(s), and has not granted (or purported to grant) any charge, lien, or other security interest with respect to the Claim(s) and the Claim Proceeds in any way, other than such payments that would become due after all payments due to the Funder under this Agreement have been satisfied in full.

5.3 No Disclosure of Common Interest Material. The Funder and its legal counsel have not disclosed any Common Interest Material to anyone without the prior written consent of the Plaintiff and has and will continue to maintain at all times during the term of this Agreement the Common Interest Material strictly confidential. The disclosure of Common Interest Material to the Funder pursuant to this Agreement will not at any time result in any waiver of the attorney-client, work product or any other legal privileges that may attach to all or any portion of such Common Interest Material under any applicable law.

5.4 Authority. The Funder is duly organized, validly existing and in good standing under the laws of its jurisdiction of organization. The Funder has the power and authority to execute and deliver this Agreement and to consummate the transactions contemplated hereby. The execution and delivery of this Agreement and the consummation of the transactions contemplated hereby have been duly authorized by all necessary corporate action on the part of the Funder and no further corporate action is required on the part of the Funder to authorize this Agreement and the transactions contemplated hereby. This Agreement has been duly executed and delivered by the Funder and constitutes the valid and binding obligations of the Funder, enforceable in accordance with its terms, subject to (a) laws of general application relating to bankruptcy, insolvency, and relief of debtors and (b) rules of law governing specific performance, injunctive relief, and other equitable remedies.

6.0 Additional Covenants

6.1 Accuracy of Representations and Warranties. Each of the Parties covenants and agrees that all of its representations and warranties made pursuant to this Agreement shall continue to be true and correct throughout the term of this Agreement. Each Party further agrees to promptly notify the other Party in the event a representation or warranty is no longer true and correct.

6.2 Duty to Cooperate. The Plaintiff covenants to cooperate in the prosecution of the Claim(s), including without limitation, that the Plaintiff will cause its officers, executives, and employees to promptly and fully assist the Lead Counsel as reasonably necessary to conduct and conclude the Claim(s). For the avoidance of doubt, such assistance includes all actions any plaintiff may reasonably expect undertaking, including, without limitation, submitting to examination, verifying statements under oath, and appearing at any Proceedings.

6.3 Duty to Conduct Claim(s). The Plaintiff covenants that it shall exercise its reasonable best efforts to continue to conduct its prosecution of the Claim(s) until their settlement or final resolution as long as the Lead Counsel continues to represent the Plaintiff on a contingency basis or the Funder continues to fund the Claim(s) in accordance with this Agreement.

6.4 Control of Claim(s). The Plaintiff shall retain control over the conduct of the Claim(s) and in particular over settlement of the Claim(s) with the Defendant. Without limiting the previous sentence, however, the Plaintiff agrees to take and follow the legal advice of the Lead Counsel at all appropriate junctures (excluding, however, the Lead Counsel's advice whether to make or accept any offer to settle the Claim(s), which shall be decided by the Plaintiff in its sole and absolute discretion).

6.5 No Interference. The Parties recognize that the Lead Counsel must at all times comply with its ethical duties to act in the best interests of the Plaintiff and in accordance with its other professional responsibilities and duties. Nothing in this Agreement entitles the Funder to interfere in the conduct of the Claim(s) and/or the Proceedings.

6.6 Duty to Inform. The Plaintiff agrees and undertakes to keep the Funder reasonably informed about the progress of the Claim(s) insofar as is proportionate, reasonably practicable, and in a manner consistent with maintaining applicable privileges and all applicable laws. In providing to the Funder any documents or information about the Claim(s) and the Proceedings, the Plaintiff does not intend to waive any privilege that may attach to such documents or information. Subject to the Funder's confidentiality obligations under this Agreement, subject to and pursuant to any applicable protective order, and subject to the Lead Counsel's reasonable judgment with respect to the preservation of all applicable legal privileges of the Plaintiff's, the Plaintiff hereby irrevocably instructs the Lead Counsel to provide written status reports to the Funder, in form and detail reasonably acceptable to the Funder, at least once each calendar quarter during the pendency of the Claim(s); upon the occurrence of any material event in the Claim(s); and from time to time upon the Funder's reasonable request. In addition, but subject to the foregoing, the Plaintiff hereby irrevocably instructs the Lead Counsel to provide to the Funder within three (3) business days following receipt a copy of any material document or filing made or obtained in the Proceedings by way of discovery, subpoena, or any other lawful means, including without limitation, the following:

6.6.1 Non-Privileged Information: The Plaintiff hereby irrevocably instructs the Lead Counsel, and if further instructions are needed, undertakes to instruct the Lead Counsel, to provide the Funder with copies or summaries of all material, non-privileged information, regardless of the information's source, confidentiality, or form, unless the Funder already possesses or controls such information.

6.6.2 Attorney Work Product: Acknowledging that this Agreement contains provisions requiring the Parties to protect the confidentiality of any Confidential Information disclosed to it and that such information includes attorney work product, the Plaintiff hereby irrevocably instructs the Lead Counsel, and if further instructions are needed, undertakes to instruct the Lead Counsel, to provide the Funder with all material attorney work product relating to the Claim as soon as practicable.

6.6.3 Attorney–Client Privileged Information: Relying on the Parties' agreement that they share a common legal interest and that communicating attorney–client privileged information to the Funder in the furtherance of that interest does not waive the privilege, the Plaintiff undertakes to share such information on a topic-by-topic basis, provided that neither the Plaintiff nor the Lead Counsel shall disclose attorney–client protected information to the Funder unless (i) the Plaintiff has discussed with the Lead Counsel the information to be shared, the reason for the sharing, and the probable consequences if the sharing is ultimately held to waive the privilege; and (ii) the Plaintiff has given written consent to such information sharing.

6.7 No Change in Lead Counsel Without Funder Notice. The Plaintiff agrees and undertakes that it will not engage a new attorney or law firm by executing a retainer agreement or other contract to employ such attorney or law firm to advise and/or represent the Plaintiff in connection with the Claim(s), without giving the Funder thirty (30) days' prior notice and without giving good faith consideration to the Funder's response, if any.

6.8 Funder Notifications of Settlement. The Plaintiff agrees that it will immediately notify the Funder upon receiving a settlement offer and provide the Funder with the complete details of the offer in such notice. The Plaintiff agrees that it will not make a settlement offer without first notifying the Funder of the proposed offer, including the complete details of the proposed offer. The Plaintiff agrees that it will not respond to a settlement offer or make a settlement offer until after giving good faith consideration to the Funder's analysis of the offer, provided that the Funder communicates its analysis within two (2) business days of receiving notice of the offer in accordance with this section. The Funder agrees to waive the right to offer analysis if the Lead Counsel and the Plaintiff determine that doing so would adversely affect their ability to come to an agreement with the Defendant. Such waivers can be called on by the Lead Counsel without notification, on a case-by-case basis. For the avoidance of doubt, the Parties acknowledge and agree that any decision regarding settlement of Claim(s), including the ultimate decision whether and for how much to settle any Claim(s), lies solely with the Plaintiff.

6.9 Indemnification. Plaintiff agrees to indemnify the Funder with respect to any and all losses or damages (including reasonable out-of-pocket and documented attorney's fees and any other costs of recovering the same) suffered by the Funder as a result of any negligence or breach of duty owed by the Lead Counsel to the Plaintiff in connection with the Claim(s) or the Proceedings, including without limitation, duties owed in connection with (a) the preparation and/or provision of (or failure to provide) any documents, materials, or information relating to the Claim(s) prior to or subsequent to the Effective Date and (b) the prosecution of the Claim(s) and/or the conduct of the Proceedings prior to or subsequent to the Effective Date. The Plaintiff agrees to cooperate with the Funder in the pursuit of any suit filed against the Lead Counsel by either the Plaintiff or the Funder in connection with such loss or damage. The indemnity in this section is limited to the extent of any successful recovery of such loss or damage or costs in any such proceedings against the Lead Counsel. The Funder shall indemnify the Plaintiff with respect to any and all losses or damages (including reasonable out-of-pocket and documented attorneys' fees and any other costs of recovering the same) suffered by the Plaintiff as a result of (i) the breach of, inaccuracy of, or failure to comply with, any of the warranties, representations or covenants of the Funder in this Agreement, including, without limitation, any damages suffered by the Plaintiffs arising out of the loss of any privilege with respect to any Common Interest Materials disclosed to the Funder pursuant to this Agreement.

6.10 Future Encumbrances. The Plaintiff shall not itself, nor shall it cause, permit, or allow, directly or indirectly, anyone else to, create, assume, incur, suffer, or permit to exist any pledge, encumbrance, security interest, assignment, lien, or charge of any kind or character on the Claim(s) without the Funder's written approval. The Plaintiff shall not itself, nor shall it cause, permit, or allow any sale sell, transfer, issue, reissue, exchange, or grant any option with respect to the Claim(s) without the Funder's written approval.

7.0 Common Interest and Confidentiality

7.1 Common Interest. The Plaintiff and the Funder agree they share a common legal interest and, to the degree necessary to further their common legal interest, agree to share Common Interest Material in accordance with the terms of this Agreement only to the extent such disclosure would not, in the sole judgment of the Lead Counsel, result in a waiver of any privilege that may attach to such Common Interest Material. The Plaintiff and the Funder agree the material would not be shared if the common legal interest did not exist. The Plaintiff and the Funder do not waive any legal professional privilege, common interest privilege, or other privilege or protection attaching to any documents and information disclosed to the Funder. Any privileged information and documents disclosed at any time to the Funder have been or will be disclosed on the additional basis that the Funder has, or will have, a common interest in the pursuit and success of the Proceedings and will at all times take all reasonable steps to maintain that privilege. It is agreed that the provision of privileged documents does not amount to any waiver of privilege, and the Funder shall not use these for any purpose other than in respect of this Agreement, except a purpose to which the Parties have consented in writing or as required by law or regulation.

7.2 Non-Disclosure Generally. During the term of this Agreement and for five (5) years following its termination, the recipient of Confidential Information of the other Party shall not disclose, use, or make available, directly or indirectly, any such Confidential Information to anyone (including, without limitation, the existence and terms of this Agreement), except as needed to perform its obligations under this Agreement, as the disclosing Party otherwise authorizes in writing, or as required by law. When disclosing, using, or making Confidential Information available in connection with the performance of its obligations under this Agreement or as permitted by the disclosing Party, the recipient shall take reasonable steps to preserve the confidentiality of the Confidential Information on terms no less restrictive than as set forth in this Agreement. The Parties agree that neither the execution of this Agreement nor the provision of Confidential Information enables the other Party to use the Confidential Information for any purpose or in any way other than as specified in this Agreement.

7.3 Potentially Enforceable Disclosure Requests. If a Party receiving Confidential Information receives a potentially enforceable request for the production of such Confidential Information, including without limitation, a subpoena or other official process, that Party will promptly notify the disclosing Party in writing, unless such notice is prohibited by law. If allowed, such notice shall be given before complying with the request and shall include a copy of the request. If the request is of the recipient of Confidential Information, and notice to the disclosing Party is prohibited by law, the recipient must make a good faith effort to contest the disclosure, if permitted under applicable law. The recipient shall also make a good faith effort to obtain an agreement protecting the confidentiality of the Confidential Information prior to disclosing it. If a disclosing Party elects to contest the request, the receiving Party shall not make any disclosure until a final, non-appealable or non-stayed order has been entered compelling such disclosure. The contesting Party shall pay its own expenses and control its contest, provided that, if the recipient contests a request when forbidden by law to give the disclosing Party notice of the disclosure request, the disclosing Party shall reimburse the recipient's reasonable expenses promptly after being notified of them.

8.0 Term

8.1 Term. The term of this Agreement shall commence on the Effective Date and terminate upon the earlier to occur of (a) the satisfaction in full of all payment obligations of the Plaintiff to the Funder pursuant to this Agreement and (b) the early termination of this Agreement pursuant to Section 8.2.

8.2 Termination. The term of this Agreement may be terminated by:

8.2.1 the mutual written agreement of the Parties;

8.2.2 either Party in the event the other Party commits a material breach of this Agreement, which breach has not been cured within ten (10) days following written notice of the breach from the non-breaching Party to the breaching Party (provided that if such breach is impossible to cure, the term may be terminated immediately upon notice of such breach to the breaching Party); or

8.2.3 by the Plaintiff upon written notice to the Funder after a failure by the Funder to fund the Costs and Disbursements as provided in this Agreement; or

8.2.4 the Funder, upon thirty (30) days advance written notice to the Plaintiff, in the event that:

(a) the Plaintiff or the Lead Counsel has made a material misrepresentation or omitted to disclose a material fact that is materially adverse to the merits of the Claim(s);

(b) the Lead Counsel is no longer actively representing the Plaintiff in the Claim(s) or the Plaintiff has provided the Funder with notice in accordance with Section 6.7 that it intends to engage a new attorney or law firm (unless the Plaintiff has obtained the Funder's prior written consent to engage the new attorney or law firm);

(c) the Funder reasonably concludes that because of a change of factual circumstances the Claim(s) is not or are not commercially viable; or

(d) there exists one or more events or a material change of circumstances that make it unlikely that the Plaintiff can recover Claim Proceeds sufficient to repay the Funder the Funder Costs Amount.

Any mutual agreement or notice of termination pursuant to this Section 8.2 shall be simultaneously provided to the Lead Counsel.

8.3 Effect of Termination. In the event the term of this Agreement is terminated pursuant to Section 8.2, the Funder shall have no further obligation to fund the reasonable Costs and Disbursements of the Plaintiff following the effective date of the termination. Any such termination by the Plaintiff shall not affect any accrued rights or entitlement of the Funder to receive the Funder Costs Amount and the Funder Recovery Amount pursuant to this Agreement. Any such termination by the Funder shall result in the proportionate reduction of the accrued rights or entitlement of the Funder to receive the Funder Costs Amount and the Funder Recovery Amount as noted above. Any termination pursuant to Section 8.2 shall not serve as a waiver of such Party's right to seek damages at law or other remedy in equity.

8.4 Survival. Sections 1, 3 (other than Section 3.1), 4, 5, 7, 8, and 9 shall survive any termination of the term of this Agreement.

9.0 Miscellaneous

9.1 Limitation of Funder's and Plaintiff's Liability. Except where directly and demonstrably caused by gross negligence or willful misconduct on the part of Funder, under no circumstances shall the Funder be liable for any outcome or disposition with respect to the Claim(s). IN NO EVENT SHALL FUNDER, PLAINTIFF, THEIR RESPECTIVE AFFILIATES OR ANY OF THEIR RESPECTIVE DIRECTORS, OFFICERS, EMPLOYEES, ATTORNEYS, OR AGENTS BE LIABLE FOR ANY INDIRECT, SPECIAL, INCIDENTAL, CONSEQUENTIAL, EXEMPLARY, OR PUNITIVE DAMAGES ARISING FROM OR DIRECTLY OR INDIRECTLY RELATED TO THE AGREEMENT, INCLUDING, WITHOUT LIMITATION, LOSS OF REVENUE, ANTICIPATED PROFITS, OR LOST BUSINESS, DATA OR SALES, OR COST OF SUBSTITUTE SERVICES, EVEN IF FUNDER OR ITS REPRESENTATIVE OR SUCH INDIVIDUAL HAS BEEN ADVISED OF THE POSSIBILITY OF SUCH DAMAGES. IN NO EVENT SHALL THE TOTAL LIABILITY OF FUNDER FOR ALL DAMAGES, LOSSES, AND CAUSES OF ACTION (WHETHER IN CONTRACT OR TORT, INCLUDING, BUT NOT LIMITED TO, NEGLIGENCE OR OTHERWISE) ARISING FROM THE AGREEMENT EXCEED, IN THE AGGREGATE, THE COMMITTED FUNDS.

9.2 Survival of Warranties. Unless otherwise set forth in this Agreement, the representations and warranties of the Parties contained herein shall survive the execution and delivery of this Agreement and shall in no way be affected by any investigation or knowledge of the subject matter thereof by or on behalf of the other Party.

9.3 Successors and Assigns. The terms and conditions of this Agreement shall inure to the benefit of and be binding upon the respective successors and assigns of the Parties, provided that the Plaintiff may not assign the rights and obligations under this Agreement without the prior written consent of the Funder.

9.4 Governing Law. This Agreement shall be governed by the internal laws of the State of California without respect to any rules regarding choice of law.

9.5 Dispute Resolution. Any dispute, claim, or controversy arising out of or relating to this Agreement or the breach, termination, enforcement, interpretation, or validity thereof, including the determination of the scope or applicability of this agreement to arbitrate, shall be determined by arbitration in San Francisco, CA before one (1) arbitrator. The arbitration shall be administered by JAMS Alternative Dispute Resolution ("JAMS") pursuant to its Comprehensive Arbitration Rules and Procedures then in effect and in accordance with the Expedited Procedures in those Rules. Service of any notice, including for service of process in any subsequent enforcement of the arbitration award in court may occur via electronic mail. The Parties agree to submit to the personal jurisdiction of California for the purposes of such arbitration, and judgment upon any award rendered in such arbitration will be binding and may be entered in any court having jurisdiction thereof.

Each Party will bear its own costs in respect of any disputes arising under this Agreement, except that the prevailing Party shall be entitled to recovery of reasonable attorney's fees in connection with any dispute that results in a total or partial judgment in favor of the prevailing Party.

9.6 Counterparts. This Agreement may be executed in two (2) or more counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument. Counterparts may be delivered via facsimile, electronic mail, or other transmission method.

9.7 Notices. All notices and other communications given or made pursuant to this Agreement shall be in writing and shall be deemed effectively given upon the earlier of actual receipt, or (a) personal delivery to the Party to be notified, (b) when sent, if sent by electronic mail or facsimile during normal business hours of the recipient, and if not sent during normal business hours, then on the recipient's next business day, (c) five (5) days after having been sent by registered or certified mail, return receipt requested, postage prepaid, or (d) one (1) business day after deposit with a nationally recognized overnight courier, freight prepaid, specifying next business day delivery, with written verification of receipt. All communications shall be sent to the respective Parties at their address as set forth on the signature page, or to such e-mail address, facsimile number, or address as subsequently modified by written notice given in accordance with this section.

9.8 Amendments and Waivers. Any term of this Agreement may be amended, terminated, or waived only with the written consent of the Parties.

9.9 Severability. The invalidity or unenforceability of any provision hereof shall in no way affect the validity or enforceability of any other provision. If any provision of this Agreement is determined to be invalid or unenforceable under applicable law and regulations by a court of competent jurisdiction, that provision shall be limited or eliminated to the minimum extent necessary so that this Agreement shall otherwise remain in full force and effect and be enforceable.

9.10 Delays or Omissions. No delay or omission to exercise any right, power, or remedy accruing to any Party under this Agreement, upon any breach or default of any other Party under this Agreement, shall impair any such right, power, or remedy of such non-breaching or non-defaulting Party nor shall it be construed to be a waiver of any such breach or default, or an acquiescence therein, or of or in any similar breach or default thereafter occurring; nor shall any waiver of any single breach or default be deemed a waiver of any other breach or default theretofore or thereafter occurring. Any waiver, permit, consent, or approval of any kind or character on the part of any Party of any breach or default under this Agreement, or any waiver on the part of any Party of any provisions or conditions of this Agreement must be in writing and shall be effective only to the extent specifically set forth in such writing. All remedies, either under this Agreement or by law or otherwise afforded to any Party, shall be cumulative and not alternative.

9.11 Force Majeure. In the event that either Party fails or is unable to perform any of its obligations under this Agreement due to any cause beyond its reasonable control, such Party shall give the other Party prompt notice of such cause, and use its reasonable best efforts to promptly correct such failure or delay in performance.

9.12 Investments Not Loans. All references in this Agreement to funding the costs and expenses of pursuing the Claim(s), however described, shall be construed to be references to Funder's investment in the Claim(s) and associated right to share in the Claim Proceeds together with the other rights set out in this Agreement, in return for its associated obligations set out in this Agreement, and it shall not be construed as a loan from the Funder to the Plaintiff or giving rise to a lender-borrower arrangement and/or relationship.

9.13 Additional Savings Clause. The Parties agree that this Agreement is not a loan and is not subject to any usury provision of the applicable state. All agreements between the Plaintiff, the Lead Counsel and the Funder are hereby expressly limited so that in no contingency or event whatsoever shall the amount paid or agreed to be paid to the Funder for the use, forbearance, or detention of the money to be funded in this Agreement exceed the maximum permissible under applicable law. If, from any circumstance whatsoever, fulfillment of any provision hereof, at the time performance of such provision shall be due, shall be prohibited by law, the obligation to be fulfilled shall be reduced to the maximum not so prohibited, and if from any circumstance the Funder should ever receive as interest (although Funder denies any "interest" is due) hereunder an amount which would exceed the highest lawful rate, such amount as would be excessive interest shall be applied to the reduction of the principal of the Agreement (against installments of principal due hereunder in the inverse order of their maturity) and not to the payment of interest. This provision shall control every other provision of all agreements between and among the Plaintiff, the Lead Counsel, and the Funder.

9.14 Advice on this Agreement. Each Party represents to the other Party that it (a) has read this Agreement; (b) has been represented in the preparation, negotiation, and execution of this Agreement by legal counsel of the Party's own choice or has voluntarily declined to seek such counsel; (c) understands the terms and consequences of this Agreement; and (d) is fully aware of the legal and binding effect of this Agreement.

9.15 Entire Agreement. This Agreement (including any exhibits or schedules thereto) constitutes the full and entire understanding and agreement between the Parties with respect to the subject matter hereof, and any other written or oral agreements relating to the subject matter hereof existing between the Parties are expressly canceled.

(*Signature Page Follows*)

IN WITNESS WHEREOF, the Parties hereto have executed this Litigation Funding Agreement as of the Effective Date.

PLAINTIFF:

DiaMedica Therapeutics Inc.

By: /s/ Rick Pauls
Name: Rick Pauls
Title: President and Chief Executive Officer
Address: 2 Carlson Pkwy, Suite 200
Minneapolis, MN 55447
E-mail: rpauls@diamedica.com

FUNDER:

LEGALIST FUND II, L.P.
By: Legalist GP II, L.L.C., its General Partner

By: /s/ Eva Shang
Name: Eva Shang
Title: Manager
Address: 880 Harrison Street
San Francisco, CA 94107
E-mail: eva@legalist.com

LEAD COUNSEL:

Fisher Broyles, LLP

By: /s/ Alfred J. Monte
Name: Alfred J. Monte
Title: Partner
Address: 1650 Market Street, 36th Fl
Philadelphia, PA 19103
Email: alfred.monte@fisherbroyles.com

List of Exhibits

Each of the following exhibits to this Litigation Funding Agreement has been omitted in accordance with Item 601(a)(5) of Regulation S-K. The registrant will furnish supplementally copies of the omitted exhibits to the SEC upon its request.

Exhibit A – Budget

Exhibit B – Wire Details

405 F.Supp.3d 612
United States District Court, D. New Jersey,
Camden Vicinage.

IN RE: VALSARTAN N-NITROSODIMETHYLAMINE (NDMA) CONTAMINATION PRODUCTS LIABILITY LITIGATION

Civil No. 19-2875 (RBK/JS)
|
Filed September 18, 2019

Synopsis

Background: In multidistrict litigation (MDL) alleging that contaminated valsartan, a generic prescription medication indicated in the treatment of high blood pressure and other conditions, contained carcinogens that caused personal injuries and economic losses, defendants, including manufacturers of active pharmaceutical ingredient (API), suppliers, repackagers, wholesalers, and retailers, requested discovery of plaintiffs' litigation funding. Plaintiffs objected.

The District Court, Joel Schneider, United States Magistrate Judge, held that plaintiffs' litigation funding was not relevant to claims against defendants, and therefore not subject to discovery.

Request denied.

Procedural Posture(s): Request for Additional Discovery.

MEMORANDUM OPINION AND ORDER

JOEL SCHNEIDER, United States Magistrate Judge

This Opinion addresses defendants' request for discovery directed to plaintiffs' "litigation funding."[1] Generally, defendants want to discover whether plaintiffs are backed by litigation funders, the details of the financing, and communications regarding the financing. The Court received defendants' letter brief [Doc. No. 189] and plaintiffs' opposition [Doc. No. 188]. The Court exercises its discretion to decide this discovery dispute without oral argument. Fed. R. Civ. P. 78; L. Civ. R. 78.1. For the reasons discussed herein, defendants' request is denied.

Background

By way of background, this Multidistrict Litigation ("MDL") concerns various FDA and voluntary recalls of contaminated valsartan, a generic prescription medication indicated in the treatment of high blood pressure and other conditions.[2] The February ***613** 14, 2019 Transfer Order of the Judicial Panel on Multidistrict Litigation is reported at In Re: Valsartan N-Nitrosodimethylamine (NDMA) Contamination Products Liability Litigation, 363 F. Supp. 3d 1378 (U.S. Jud. Pan. Mult. Lit. 2019). Plaintiffs generally allege defendants' valsartan contained carcinogens that caused personal injuries and economic losses. Defendants deny their drugs caused any injuries or damages, although it is not disputed that at least some of defendants' drugs were contaminated. Presently approximately 60 defendants are named. These defendants include manufacturers of the active pharmaceutical ingredient ("API"), suppliers, repackagers, wholesalers, and retailers. Some of the "lead" defendants, API manufacturers, are located in China and India. Given the number of potential plaintiffs, the amount in dispute, the seriousness of plaintiffs' claimed injuries, and the fact that some "target" defendants are located overseas, this MDL will undoubtedly be costly to prosecute and defend.

Since the first case management conference in March, 2019, much has been done to organize and manage the case. This includes designating and approving the parties' leadership structure (CMO No. 6, Doc. No. 96), and identifying the "core discovery" to be produced by defendants (April 29, 2019 Order, Doc. No. 88).[3] In June, 2019, three consolidated "master complaints" were filed. These complaints generally grouped plaintiffs into three categories. The first master complaint addresses the claims of individual plaintiffs [Doc. No. 122] who allege they contracted various forms of cancer from consuming defendants' contaminated valsartan. To date approximately 126 personal injury cases of this type have been filed. Plaintiffs' counsel estimates approximately 2,000 cases may eventually be filed. The second master complaint [Doc. No. 123] is a nationwide medical monitoring class action filed on behalf of all "individuals who consumed [contaminated] generic valsartan-containing drugs ... at least since January 1, 2012[.]" Id. at ¶390. The potential class size is undoubtedly in the tens of thousands. The third master complaint (Doc. No. 121) is a nationwide economic class action filed on behalf of "[a]ll individuals and entities ... who,

since at least January 1, 2012 to the present, paid any amount of money for a valsartan-containing drug [.]" Id. at ¶413. This class size is also expected to be very large.

To date, no formal discovery has been directed to plaintiffs. The Court expects to shortly approve "Fact Sheets" to be answered by all personal injury plaintiffs and the named class representatives. As to defendants, the "lead" parties have already produced most of what has been denominated as "core discovery."

The present discovery dispute arose in the context of what questions would be included in plaintiffs' Fact Sheet to be ***614** answered. Specifically, defendants propose to require each plaintiff to produce the following: "all documents and communications related to funding or financing, if any, you or your counsel have obtained to pursue this litigation." [4] Defendants' letter brief identifies precisely what they want:

> Defendants seek to obtain information about Plaintiffs' agreements and communications with any third-party funders of the litigation, including Plaintiffs' documents and communications relating to or concerning any litigation finance obtained in connection with this litigation, documents and communications regarding conferences, meetings or conventions attended with the purposes of seeking litigation finance, and documents and communications relating to agreements to finance this litigation.

DLB at 1.

Not unexpectedly, plaintiffs object to producing discovery regarding their litigation funding. Albeit, plaintiffs are willing to produce some documents for an in camera review. Plaintiffs argue their private financial information is irrelevant to their claims and defenses and defendants have "no legitimate need for the requested information." Plaintiffs' Letter Brief ("PLB") at 2. Plaintiffs, however, agree to submit documents to the Court for an in camera review, "where the litigation funding company has control or input into litigation decisions, including settlement, which could interfere with a plaintiff's control of his, or her lawsuit and the attorney-client relationship." Id.

Defendants disagree with plaintiffs and contend "third-party funding represents a critical piece of information to which Defendants are entitled." DLB at 1. Defendants argue the requested discovery is relevant to identifying, "the real party in interest as to some or all of the claims alleged in this action," and whether plaintiffs have standing to sue. Id. Defendants also argue plaintiffs' funding information is relevant to determining: (1) plaintiffs' credibility and bias, (2) the scope of proportional discovery, (3) the scope of potential sanctions, and (4) the "medical necessity and the reasonableness of plaintiff's treatments." Id. at 2. Defendants argue, "[t]he recent history of mass tort multi-district litigation is littered with examples of undisclosed non-party involvement gone wrong to the detriment" of the legal process and public health. Defendants also argue that "courts and legislators lean toward mandating disclosure of third-party funding." Id. at 4.

Discussion

This is not the first instance, nor likely the last, where defendants in a MDL mass tort case seek discovery directed to plaintiffs' litigation funding. Scores of courts and commentators have already addressed the issue. This Court can add little to the existing discourse and is left to essentially parrot what has already been written. At bottom, courts are split on the issue and plaintiffs and defendants can each cite to cases supporting their positions. What is not in dispute is that there is no binding Third Circuit precedent on whether a plaintiff's litigation funding is a proper subject of discovery. Nor is the Court aware of any published New Jersey District Court authority on point. [5]

***615** 1. As to Relevance, Plaintiffs Have the Better Argument

After considering the present record and the relevant case law, the Court rules in plaintiffs' favor. The Court finds that litigation funding is irrelevant to the claims and defenses in the case and, therefore, plaintiffs' litigation funding is not discoverable.

The scope of relevant discovery is set forth in Fed. R. Civ. P. 26(b)1). This Rule permits discovery regarding, "any nonprivileged matter that is relevant to any party's claim or defense and proportional to the needs of the case[.]" The Court agrees with the plethora of authority that holds

that discovery directed to a plaintiff's litigation funding is irrelevant. See Benitez v. Lopez, 17-CV-3827-SJ-SJB, 2019 WL 1578167, at *1 (E.D.N.Y. March 14, 2019) ("As to the litigation funding documents, Defendants fail to establish that such discovery is 'relevant to any party's claims or defense.' " Also stating, "[t]he financial backing of a litigation funder is as irrelevant to credibility as the Plaintiff's personal financial wealth, credit history, or indebtedness. That a person has received litigation funding does not assist the factfinder in determining whether or not the witness is telling the truth."); Miller UK Ltd. v. Caterpillar, Inc., 17 F. Supp.3d 711, 742 (N.D. Ill. 2014) ("Caterpillar is not entitled to discover the amount of money sought or received by Miller, the details of the agreement it has with its funder, or how much the funder will receive if Miller wins the case. In the setting of this case, that information is simply irrelevant."); Kaplan v. S.A.C. Capital Advisors, L.P., S.A.C., No. 12-CV-9350 (VM)(KNF), 2015 WL 5730101, at *5 (S.D.N.Y. Sept. 10, 2015), aff'd, 141 F. Supp. 3d 246 (S.D.N.Y. 2015). (denying defendants' request for plaintiffs' litigation funding documents on the ground that "defendants did not show that the requested documents are relevant to any party's claim or defense."); Space Data Corp. v. Google LLC, Case No. 16-cv-03260 BLF, 2018 WL 3054797, at *1 (N.D. Cal. June 11, 2018) (denying litigation funding discovery and stating, "[t]he Court is not persuaded that the materials sought are relevant to any party's claim ...."); MLC Intellectual Property LLC v. Micron Technology, Inc., Case No. 14-cv-3657-SI, 2019 WL 118595, at *2 (N.D. Cal. Jan. 7, 2019) (denying litigation funding discovery and stating, "[t]he Court concludes that [defendant] is not entitled to the discovery it seeks because it is not relevant."); Yousefi v. Delta Electric Motors, Inc., No. 13-CV-1632 RSL, 2015 WL 11217257, at *2 (W.D. Wash. May 11, 2015) ("[w]hether plaintiff is funding this litigation through savings, insurance proceeds, a kickstarter campaign, or contributions from [a] union is not relevant to any claim or defense at issue.").

To be sure, the Court is not ruling that litigation funding discovery is off-limits in all instances. In cases where there is a showing that something untoward occurred, the discovery could be relevant. In other words, rather than directing carte-blanche discovery of plaintiffs' litigation funding, the Court will Order the discovery only if good cause exists to show the discovery is relevant to claims and defenses in the case. For example, discovery will be Ordered where there is a sufficient showing that a non-party is making ultimate litigation or settlement decisions, the interests of plaintiffs or the class are sacrificed or are not being protected, or conflicts of interest exist. However, no such evidence has been raised by defendants and, to date, the Court has not seen anything of the sort.

Although defendants raise a parade of horribles that could or may arise from litigation funding agreements, none has occurred ***616** here. Nor is there any reason to believe that anything untoward will occur in the future. The fact that defendants have raised no nonspeculative basis for their discovery request results in its denial. Kaplan, 2015 WL 5730101, at *5; see also VHT, Inc. v. Zillow Group, Inc., Case No. C15-1096 JLR, 2016 WL 7077235, at *1 (W.D. Wash. September 8, 2016)(denying litigation funding discovery "[w]ithout some objective evidence that any of [defendant's] theories of relevance apply to [the] case."); see also In Re: Riddell Concussion Reduction Litigation, C.a. No. 13-7585 (JBS/JS), 2016 WL 7325512, at *3 (D.N.J. Jan. 19, 2016) (discovery of the class representatives' fee agreements denied on the ground that the defendant's arguments were "speculative and insufficient to demonstrate the relevance of the sought-after fee agreements.").

Even if plaintiffs' litigation funding is marginally relevant, which is not the case, defendants' requested discovery would be denied because it is not "proportional to the needs of the case." Rule 26(b)(1); Space Data Corp., 2018 WL 3054797, at *1 (emphasis in original) ("[e]ven if litigation funding were relevant (which is contestable), potential litigation funding is a side issue at best. The Court finds that there is much discovery that would be more ... important in resolving the merits of this case."); Miller UK Ltd., 17 F.Supp. 3d at 721 (discovery was never "intended to be an excursion ticket to an unlimited exploration of every conceivable matter that captures an attorney's interest.").

The parties have just begun to scratch the surface regarding discovery directed to the important issues in the case. Plaintiffs' Fact Sheets are not finalized and defendants have only produced core and not complete Rule 26 discovery. Plaintiffs' litigation funding is a "side issue" that has nothing to do with addressing the key issues in the case such as what caused defendants' valsartan contamination, whether the contamination caused any injuries, and whether plaintiffs may recover under their theories of liability. Unless and until defendants make a legitimate showing that plaintiffs' litigation funding is directed to a relevant issue, which has not been done, the discovery is denied. VHT, Inc., 2016 WL 7077235, at *1 (denying motion to compel the identity of any litigation funder on the ground that the requested discovery

was "negligibly relevant, minimally important in resolving the issues[,] and unduly burdensome," and was therefore "disproportional to the needs of the case."). [6]

2. Defendants' Authority and Arguments are Not Persuasive

Defendants' argument that plaintiffs' litigation funding is not only relevant but a "critical piece of information" is flatly rejected. DLB at 1. It is pure speculation to argue a potential litigation funder rather than the named plaintiff may be the real party in interest. Id. at 1-2. Defendants have not cited any evidence that a "third-party owns the rights to [this] action." Id. at 2. This is not a patent case where the ownership of a patent is relevant to determining who has standing to bring the lawsuit. See ***617** Cobra International, Inc. v. BCNY International, Inc., No. 05-61225, 2013 WL 11311345, at *3 (S.D. Fla. Nov. 4, 2013). Also, despite their protestations, defendants have not cited to a single instance where a litigation funder owned the right to recover rather than being a passive investor that shares in the benefit of a recovery from an attorney's contingent fee.

Defendants' argument that plaintiffs' litigation funding is relevant to credibility and bias (DLB at 2) is misplaced. Plaintiffs are not seeking to identify who is paying the legal fees of a key witness. See Berger v. Seyfarth Shaw, LLP, No. C07-05279 JSW, 2008 WL 4570687, at *1 (N.D. Cal. Oct. 14, 2008); Bryant v. Mattel, 573 F. Supp. 2d 1254, 1274 (C.D. Cal. 2007).

In addition, the Court rejects the notion that it must know the details of plaintiffs' funding arrangements to decide the scope of discovery, the outcome of discovery cost-shifting, and the proper assessment of sanctions. DLB at 2. The Court routinely decides these issues without inquiring as to how the parties finance their cases. If the Court accepted defendants' argument, the source(s) of defendants' assets and funding could become fair game for discovery. The Court has no intention of going down this "rabbit hole."

Defendants cite to Orders in another MDL where the Court directed discovery of funding information to "inform discussions of medical necessity and the reasonableness of plaintiff's treatments." DLB at 2. See In re: American Medical Systems, Inc. Pelvic Repair Systems Product Liability Litigation, MDL No. 2325, at 12-14, 2016 WL 3077904 (S.D.W. Va. May 31, 2016), Pretrial Order # 215 (Motion to Modify Subpoena or for Protective Order of Nonparties Surgical Assistance and Black Barber). Defendants cite to this Order to support their argument that, "failure to disclose [litigation funding] information can undermine and derail the MDL." DLB at 1. However, unlike the pelvic mesh litigation, there is no contention here that any contrived or unnecessary medical treatment occurred. Nor is there a scintilla of evidence, as may have existed in the other MDL's defendants cite to (silicone breast litigation (1990's), diet drug litigation (early 2000's), and mesh litigation) that inappropriate or fraudulent diagnoses or treatment occurred.

The Court disagrees with defendants' statement that there is a "shifting tide towards disclosure of third-party litigation funding information in courts ... coupled by a similar movement in the legislative realm." DLB at 5. This Opinion cites to substantial recent authority denying disclosure. Benitez, supra; MLC Intellectual Property, supra; Space Data Corp., supra. Further, the disclosure requirement in the Local Rules for the N.D. Cal. is limited to class actions. And, this adoption was not followed by a groundswell of copycats, including New Jersey. [7]

***618** The case law defendants rely upon is not persuasive. In Cobra International, Inc., supra, in the context of a dispute over the ownership of a patent, the court wrote that discovery regarding a litigation funding agreement was "relevant and is not privileged[.]". 2013 WL 11311345, at *3. This litigation does not concern the ownership of a patent. In Acceleration Bay LLC v. Activision Blizzard, Inc., C.A. No. 16-453-RGA, 454-RGA and 455-RGA, 2018 WL 798731 (D. Del. February 9, 2018), the Court adopted a Special Master's recommendation that plaintiff produce emails and documents plaintiff provided to a litigation funder and its counsel. The Court simply stated, "I agree with defendants that the communications are relevant." Id at *3. In Acceleration Bay, however, unlike this case, the defendants argued the requested litigation funding documents were relevant to "central issues like validity and infringement, valuation, damages, royalty rates, pre-suit investigative diligence, and whether [Plaintiff] is an operating-company[.]" Id. at *3. In Berger, supra, the Court reversed a Magistrate Judge's ruling denying discovery of the fee-payment arrangements of a key witness. 2008 WL 4570687, at *1. The Court ruled the discovery was relevant to the credibility and bias of a witness. Id. at *1. This is not a present concern of defendants.

Defendants' reliance on In Re: American Medical Systems, Inc., MDL No. 2325, 2016 WL 3077904 (S.D.W.Va. May 31, 2016), is misplaced. That case is a MDL involving AMS's pelvic mesh products. During the course of discovery

AMS learned that some of the plaintiffs had corrective surgery arranged and funded through third-party funding companies. AMS then served subpoenas on the companies seeking documents relating to the plaintiffs' funding. As to the documents the Court held were discoverable, the Court ruled they were relevant to understanding the plaintiffs' "motivation" to undergo corrective surgeries. Id. at *5. The documents were also relevant to learning if the plaintiffs were "pressed" to undergo corrective surgeries and the "reasonableness of the costs associated with the corrective surgeries that the plaintiffs underwent." Id. at *5. The AMS case is not remotely analogous to this litigation. To date, defendants have not even hinted at the fact that litigation funders may be funding plaintiffs' treatment. There is also no evidence that third-party funders may be unreasonably padding plaintiffs' damage claims. At this stage of the case, any argument to this effect is pure speculation.

Last, defendants' reliance on Gbarabe v. Chevron Corp., Case No. 14-CV-00173-SI, 2016 WL 4154849 (N.D.Cal. August 5, 2016), is also misplaced. In Gbararbe, plaintiffs' counsel represented a class of approximately 12,600 Nigerian individuals allegedly damaged by a 2012 drilling explosion off the coast of Nigeria. Plaintiffs' lawyers were solo practitioners who acknowledged they were dependent on outside funding to prosecute the case. Id. at *1. The lawyers also conceded the relevance of their funding agreement. Id. The Court ruled that, "under the circumstances of [the] case, the litigation funding agreement is relevant" to the adequacy of representation in the case. Id. Here, plaintiffs do not concede the relevancy of defendants' requested discovery. In addition, the Court has previously ruled that as a general matter a class action plaintiff's finances are off-limits to discovery. See Riddell, supra.

3. In Camera Review

As a coda to this Opinion, the Court will address plaintiffs' offer that the ***619** Court review their litigation funding documents in camera, "where the litigation funding company has control or input into litigation decisions, including settlement, which could interfere with a plaintiff's control of his or her lawsuit and the attorney-client relationship." PLB at 2. The Court agrees to this review with one proviso. That is, that the Court relies on plaintiffs' counsel to exercise their best professional judgment when the review should occur. After all, plaintiffs' counsel, not the Court, knows the details of their contractual relationship. If a good faith question exists as to whether documents should be submitted for review, the Court expects counsel to err on the side of disclosure. [8] The Court is aware that a respected jurist in a pending MDL has Ordered an ex parte in camera review in all instances where an attorney has obtained third-party contingent litigation financing. Opiate Litigation, supra. However, the course this Court chooses to take is not to require automatic review but to leave it to plaintiffs' counsel to decide when the Court should be involved. As this Court wrote in Montana v. County of Cape May Board of Freeholders, C.A. No. 09-755 (NLH/JS), 2013 WL 11233748, at *8-9 (D.N.J. Sept. 20, 2013) (citations and quotations omitted):

> The rules of discovery must necessarily be largely self-enforcing. The integrity of the discovery process rest on the faithfulness of parties and counsel to the rules – both the spirit and the letter. Moreover, the discovery provisions of the Federal Rules are meant to function without the need for constant judicial intervention, and ... those rules rely on the honesty and good faith of counsel in dealing with adversaries.

Defendants are not left out of this process. If defendants have good cause to believe the criteria for an in camera review is met, the Court will consider their application. What will not be Ordered is the automatic or carte blanche review of all litigation funding agreements and documents. [9] Speculation does not justify discovery. Benitez, 2019 WL 1578167, at *1.

CONCLUSION

In sum, the Court denies defendants' request for carte blanche discovery of plaintiffs' litigation funding as the discovery is irrelevant to the claims and defenses in the case. At best, the discovery is a side issue that does not help advance this complex litigation. To date, the litigation has run smoothly without the requested discovery and the Court expects this to remain the case. Defendants' parade of horribles that might occur from litigation funding is pure speculation. To be sure, however, the Court is not ruling that plaintiffs' litigation funding can never be discovered. ***620** If good cause exists to order the discovery in an appropriate instance, it will be done. What the Court will not do is Order the discovery in the absence of a demonstratable showing that the discovery is

relevant to a claim or defense in the case. That showing has not been made to date.

ORDER

Accordingly, for all the foregoing reasons, **IT IS HEREBY ORDERED** this 18th day of September, 2019, that defendants' request that plaintiffs' litigation funding be included in plaintiffs' Fact Sheets is DENIED; and it is further

ORDERED that to the extent the request is made that the Court Order the automatic or carte blanche disclosure of plaintiffs' litigation funding agreements and documents, the request is DENIED; and it is further

ORDERED the Court will review in camera plaintiffs' litigation funding documents where plaintiffs' counsel makes this request or if good cause exists to believe a litigation financer has control or input into plaintiffs' litigation decisions, including settlement, which would interfere with a plaintiff's control of his or her lawsuit and the attorney-client relationship, or other good cause exists for the review. The Court will thereafter determine the scope of discovery, if any.

All Citations

405 F.Supp.3d 612

Footnotes

1 Litigation financing in the MDL context, "refers to any agreement under which any person, other than an attorney, permitted to charge a contingent fee representing a party, has a right to receive compensation that is contingent on and sourced from any proceeds of an MDL." In re: National Prescription Opiate Litigation("Opiate Litigation"), Case No. 1:17-MD-2804, 2018 WL 2127807, at *1 (N.D. Ohio May 7, 2018). The Court does not presently know whether any plaintiff has an arrangement with a litigation funder.

2 The recalls at issue started in 2018 and continued into 2019. The Court understands plaintiffs recently filed a Motion to Transfer and Expand the Scope of MDL 2875 with the Judicial Panel on Multidistrict Litigation to include "all Federal cases concerning Angiotensin Receptor Blockers ("ARB's") contaminated with carcinogenic contaminants." Defendants' September 11, 2019 Letter Brief ("DLB") at 5, Doc. No. 213. Plaintiffs recently clarified that their present intention is only to expand the MDL to include contaminated losartan and irbesartan.

3 The Court defined "core discovery" as discovery that is, "(1) easily identifiable, (2) unquestionably relevant and not privileged, (3) relatively simple to retrieve, and (4) discrete." See April 29, 2019 Order at l n. 1, Doc. No. 88. The purpose of this early production was to focus the parties' efforts on key issues, to enable plaintiffs to promptly and efficiently identify the relevant ESI and documents to request, and to reduce the likely substantial cost of defendants' ESI production.

4 As is apparent, defendants asks for litigation funding discovery from plaintiffs and their attorneys.

5 In Mershon v. Elastic Stop Nut Div. of Harvard Industries, Inc., C.A. No. 87-1319 (HLS), 1990 WL 484152, at *12 (D.N.J. March 23, 1990) (citation omitted), the Court merely stated, "[t]hird party funding, in and of itself, does not make the named plaintiffs antagonistic to the interests of the class." The decision did not address a discovery issue.

6 Defendants implicitly posit that plaintiffs' litigation financing could create perverse financial incentives to sacrifice the client's best interests. However, as one commentator has noted, "[l]itigation financing is no different ... than the risks presented by hourly and contingency fees, both of which create their own

characteristic misalignment of interests." W. Bradley Wendel, Paying the Piper but not Calling the Tune: Litigation Financing and Professional Independence, 52 Akron L. Rev. 1, 47 (2019).

7 One of the primary reasons jurisdictions may have adopted a disclosure requirement is to assist judges with regard to possible recusal or disqualification decisions. Defendants have not raised this as a reason to require disclosure here. In addition, in view of the Court's ruling that plaintiffs' litigation funding is off-limits because of relevancy and proportionality concerns, the Court does not have to decide if the discovery is protected by the work-product doctrine. However, the Court notes the weight of recent authority appears to lean in this direction. Odyssey Wireless, Inc. v. Samsung Electronics Co., Ltd, Case No. 3:15-CV-01738-H (RBB), 2016 WL 7665898 at *4-5 (S.D. Cal. Sept. 20, 2016); United States v. Homeward Residential, Inc., Case No. 4:12-CV-461, 2016 WL 1031154, at *6 (E.D. Tex. Mar. 15, 2016); Viamedia, Inc. v. Comcast Corp., Case No. 16-CV-05486, 2017 WL 2834535, at *3 (N.D. Ill. June 30, 2017); Morley v. Square, Inc., Case No. 4:140CV172, 2015 WL 7273318, at *2 (E.D. Mo. Nov. 18, 2015); Doe v. Soc'y of the Missionaries of the Sacred Heart, No. 11-CV-02518, 2014 WL 1715376 at *3 (N.D. Ill. May 1, 2014); Miller, 17 F. Supp. 3d at 738; see also Opiate Litigation, 2018 WL 2127807, at *1; but see Acceleration Bay LLC, 2018 WL 798731, at *2-3.

8 Some of the questions counsel should consider are: (1) whether the funder has formal or de facto control over litigation decisions?; (2) whether funding may be withdrawn, and if so when?; (3) whether the funder decides when to settle a case?; and (4) whether the funder has control over the selection of counsel? See Bert I. Huang, Litigation Finance: What do Judges Need to Know? 45 Colum. J.L. & Soc. Probs. 525, 529-32 (2012).

9 Some of the information the Court will consider to decide if an in camera review is appropriate is whether the litigation is unduly prolonged and if settlement or ADR is discouraged, whether counsel's control over the litigation is undercut, if settlement money is unduly directed away from a plaintiff, if the attorney-client relationship is compromised, or if the professional independence of an attorney is diminished. See also Huang, supra. Although it may not be directly on point, New Jersey RPC 5.4(c) provides that a "lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services." It is not clear if a litigation funder fits into the class of persons covered by this RPC.

End of Document

Lawsuit Funding LLC v Lessoff
2013 NY Slip Op 33066(U)
December 4, 2013
Sup Ct, New York County
Docket Number: 650757/2012
Judge: Eileen Bransten

SUPREME COURT OF THE STATE OF NEW YORK – NEW YORK COUNTY
PRESENT: Hon. Eileen Bransten, Justice PART 3

----------X

LAWSUIT FUNDING LLC, and LAWSUIT CAPITAL ADVISORS, LLC,

Plaintiffs,

- *against* -

JEFFREY LESSOFF and THE LAW FIRM OF JEFFREY LESSOFF,

Defendants.

----------X

Index No.: 650757/2012
Motion Date: 07/23/13
Motion Seq. No.: 002

The following papers, numbered 1 to 3, were read on this motion for Summary Judgment.

Notice of Motion/Order to Show Cause - Affidavits - Exhibits No(s). 1

Answering Affidavits - Exhibits No(s). 2

Replying Affidavits No(s). 3

Cross-Motion: X Yes ☐ No

Upon the foregoing papers, it is ordered that this motion is

DECIDED IN ACCORDANCE WITH THE ACCOMPANYING MEMORANDUM DECISION.

Dated: December 4, 2013

Eileen Bransten, J.S.C.
Hon. Eileen Bransten

MOTION/CASE IS RESPECTFULLY REFERRED TO JUSTICE
FOR THE FOLLOWING REASON(S):

1. CHECK ONE: .....☐ CASE DISPOSED X NON-FINAL DISPOSITION

2. CHECK AS APPROPRIATE: Motion Is: ☐ GRANTED ☐ DENIED X GRANTED IN PART ☐ OTHER

3. CHECK AS APPROPRIATE: Cross-Motion Is: ☐ GRANTED ☐ DENIED X GRANTED IN PART ☐ OTHER

4. CHECK IF APPROPRIATE: .....☐ SETTLE ORDER ☐ SUBMIT ORDER

☐ DO NOT POST ☐ FIDUCIARY APPOINTMENT ☐ REFERENCE

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: IAS PART THREE

----------X

LAWSUIT FUNDING, LLC, and LAWSUIT CAPITAL ADVISORS, LLC,

Plaintiffs,

- *against* -

JEFFREY LESSOFF and THE LAW FIRM OF JEFFREY LESSOFF,

Defendants.

----------X

Index No. 650757/2012
Motion Date: 07/23/2013
Motion Seq. No.: 002

BRANSTEN, J.

This case, involving alternative litigation financing, comes before the Court on Plaintiff Lawsuit Funding, LLC ("Funding") and Plaintiff Lawsuit Capital Advisors, LLC's ("Advisors," collectively, "Plaintiffs") motion for partial summary against Defendant Jeffrey Lessoff and Defendant The Law Firm of Jeffrey Lessoff (collectively, "Defendants"). Defendants oppose and cross-move for leave to amend their Answer to assert a statute of limitations defense and to dismiss the Complaint. For the reasons stated below, Plaintiffs' motion is granted, as to liability, and Defendants' cross-motion is granted, in part, and denied, in part.

Background[1]

Defendant Lessoff is an attorney, admitted to practice law in New York, who receives legal fees on a contingency basis. (Plaintiffs' Rule 19-a Statement of Undisputed Facts ("Stat.") ¶¶ 2, 3.) On January 16, 2007, Defendants entered into a litigation-funding agreement with Plaintiffs entitled "Sale of Contingent Proceeds Agreement" (the "Sale Agreement"). (Stat. ¶ 3.) The Sale Agreement called for Plaintiffs to receive a portion of the contingent legal fee that Defendants were expected to receive if five specifically named lawsuits were adjudicated in favor of Defendants' clients. (Affirmation of Matthew S. Aboulafia in Support of Plaintiffs' Motion ("Aboulafia Affirm.") Ex. C.) In exchange, Defendants received $108,500 as an advance on those expected legal fees. (Aboulafia Affirm. Ex. C.)

Defendant Lessoff failed to make any payments under the Sale Agreement. (Stat. ¶ 5.) On November 14, 2008, Plaintiff Funding filed an arbitration claim, pursuant to the Sale Agreement, seeking to compel Lessoff to surrender legal fees received in connection with the five named lawsuits. (Aboulafia Affirm. Ex. F at 1.) Lessoff unsuccessfully attempted to stay the arbitration. (Aboulafia Affirm. Ex. F at 1.) In August 2009,

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[1] Some facts in this section are derived from Plaintiffs' Rule 19-a Statement of Undisputed Facts. Due to Defendants' failure to submit a counter-statement, Plaintiffs' 19-a Statement has been deemed admitted in its entirety by Defendants for purposes of this motion. *See* 22 N.Y.C.R.R. § 202.70 (Rule 19-a(d)). The remaining facts are derived from the Affirmation of Matthew S. Aboulafia in Support of Plaintiffs' Motion.

Funding and Lessoff settled the arbitration claim with a Stipulation of Settlement ("Stipulation") and a Consent Award ("Award"). (Aboulafia Affirm. Ex. F.)

In the Stipulation, Defendants acknowledged that they received $48,000 in legal fees from a named lawsuit and failed to pay Plaintiffs. (Aboulafia Affirm. Ex. F at 3 n.1.) Further, Defendants agreed to pay $7,000 plus interest to Advisors within two years of signing the Stipulation, as well as to pay Funding up to $238,700 based on legal fees Defendants expected to receive from eight specifically named lawsuits. (Aboulafia Affirm. Ex. F at 3.) Defendants also agreed to pay 25% of any other legal fees received from unrelated cases until the $108,500 advancement was fully paid. The Stipulation additionally provided that Defendants would pay $5,000 in liquidated damages, attorney's fees and other collection fees if they defaulted on the Stipulation. (Aboulafia Affirm. Ex. F at 3.) Finally, the Stipulation stated that the Award would not be final, and Plaintiffs would not be entitled to confirm the Award, until Defendants defaulted under the Stipulation. (Aboulafia Affirm. Ex. F at 4.)

In August 2011, Defendants defaulted under the Stipulation by failing to pay the $7,000 owed to Advisors. (Stat ¶ 12.) Plaintiffs commenced this action on March 12, 2012, seeking to enforce the Sale Agreement and the Stipulation. The Complaint asserts (i) that the Law Firm of Jeffrey Lessoff breached the Sale Agreement; (ii) that Jeffrey Lessoff personally breached the Sale Agreement; (iii) that Jeffrey Lessoff and the Law

Firm of Jeffrey Lessoff damaged Advisors by breaching the Stipulation; and (iv) that Jeffrey Lessoff and the Law Firm of Jeffrey Lessoff damaged Funding by breaching the Stipulation.

On June 5, 2012, Plaintiffs served Defendants with a Notice to Admit, pursuant to CPLR 3123, seeking admissions regarding the attorney's fees in the eight cases delineated in the Stipulation. Defendants failed to respond to the Notice to Admit.

Plaintiffs now move for partial summary judgment on their third and fourth causes of action, seeking to enforce the terms of the Stipulation against Defendants. Defendants oppose the motion and cross-move to amend their Answer to assert a statute of limitations defense, and to dismiss the Complaint.

Analysis

I. Defendants' Cross-Motion for Leave to Amend

Pursuant to CPLR 3025(b), leave to amend should be freely given. However, leave to amend may be denied if there is either "prejudice or surprise resulting directly from the delay," or if the proposed amendment "is palpably improper or insufficient as a matter of law." *McGhee v. Odell*, 96 A.D.3d 449, 450 (1st Dep't 2012) (internal citations omitted).

Defendants propose to amend their Answer to assert a statute of limitations defense. Defendants argue that the statute of limitations to confirm an arbitration award is one year, and that over one year has passed since the Award was rendered. In essence, Defendants contend that Plaintiffs' motion for summary judgment to enforce the Stipulation is an attempt to confirm the Award and circumvent the one-year statute of limitations.

Under New York law, "a stipulation is an independent contract which is subject to the principles of contract law." *Adelsberg v. Amron*, 103 A.D.3d 571, 572 (1st Dep't 2013). Therefore, the Stipulation is not subject to the one-year statute of limitations for confirmation of awards, but rather the six-year statute for contracts. *See* CPLR § 213. The parties entered into the Stipulation in August 2009, and Plaintiffs commenced this action in 2012. Plaintiffs commenced this action within the six-year statute of limitations, and the portion of Defendants' cross-motion seeking leave to amend is denied as palpably insufficient.

II. Summary Judgment Standard

The standards for summary judgment are well-settled. The movant must tender evidence, by proof in admissible form, to establish the cause of action "sufficiently to warrant the court as a matter of law in directing judgment." CPLR 3212(b); *Zuckerman*

v. City of New York, 49 N.Y.2d 557, 562 (1980). "Failure to make such showing requires denial of the motion, regardless of the sufficiency of the opposing papers." *Winegrad v. New York Univ. Med. Ctr.*, 64 N.Y.2d 851, 853 (1985). Once such proof has been offered, to defeat summary judgment "the opposing party must show facts sufficient to require a trial of any issue of fact." CPLR 3212(b); *Zuckerman*, 49 N.Y.2d at 562.

III. Defendants' Cross-Motion for Summary Judgment

Defendants move for summary judgment against the entire Complaint. Based upon the doctrine of release, Defendants are entitled to summary judgment on the first and second causes of action that seek to enforce the Sale Agreement. The first paragraph of the Stipulation states that the "Stipulation . . . settles any and all claims that [Plaintiffs] and [Defendants], as the parties to the present arbitration proceeding, had, have or may have in the future against each other arising out of or relating to the [Sale Agreement]." *See* Aboulafia Affirm. Ex. F at 1.

"A release 'is a jural act of high significance without which the settlement of disputes would be rendered all but impossible' . . . It is well established that further litigation following a release should not be permitted 'except [to prevent] . . . a grave injustice.'" *See Gibli v. Kadosh*, 279 A.D.2d 35, 38 (1st Dep't 2000) (quoting *Mangini v. McClurg*, 24 N.Y.2d 556, 563 (1999)). Therefore Defendants are entitled to summary

judgment on the Complaint's first and second causes of action regarding the Sale Agreement.

IV. Plaintiffs' Motion for Partial Summary Judgment

Plaintiffs' motion for partial summary judgment on the third and fourth causes of action seeks to enforce the Stipulation against Defendants and seeks additional discovery to discern Plaintiffs' full amount of damages. Plaintiffs submit the Stipulation and the unanswered Notice to Admit, showing that Defendants breached their obligations under the Stipulation.

The elements of a breach of contract claim are "the existence of a contract, the plaintiff's performance thereunder, the defendant's breach thereof, and resulting damages." *Harris v. Seward Park Housing Corp.*, 79 A.D.3d 425, 426 (1st Dep't 2010). Plaintiffs have demonstrated, and Defendants do not contest, the existence of a contract, the Stipulation, because "a stipulation is an independent contract which is subject to the principles of contract law." *Adelsberg v. Amron*, 103 A.D.3d 571, 572 (1st Dep't 2013). Further, Plaintiffs have shown that they performed under the contract by paying Defendants $108,500. *See* Stat. ¶ 3. Finally, Plaintiffs have shown that Defendants did not perform and that Plaintiffs have been damaged thereby. *See* Stat. ¶ 5 ("Defendant has obtained settlements in all the actions covered by the [Sale Agreement] . . . but has failed

to pay"). Therefore, Plaintiffs have carried their burden to submit proof, in admissible form, entitling them to summary judgment.

Defendants make four arguments against Plaintiffs' summary judgment motion. First, Defendants argue that the Notice to Admit cannot be used in support of Plaintiffs' motion for summary judgment. Second, Defendants contend that the transactions at issue here are usurious loans that cannot be enforced by the Court. Third, Defendants argue that Plaintiffs are non-lawyers seeking to improperly share attorney's fees. Finally, Defendants contend that the Sale Agreement and Stipulation are unconscionable.

1. *Admissions*

First, Defendants argue that the Notice to Admit cannot be used to grant summary judgment to Plaintiffs and that "Plaintiff must prove his case." *See* Affirmation of Jeffrey L. Lessoff in Opposition to Cross-Motion ("Lessoff Affirm.") ¶ 3. However, failure to timely respond to a notice to admit results in admitting the facts contained therein. *See* CPLR § 3123(a); *Hernandez v. City of New York*, 95 A.D.3d 793, 794 (1st Dep't 2012) ("Defendant is deemed to have admitted the facts contained in plaintiff's notice to admit, as it did not timely respond to the notice"). Therefore, Defendants have admitted, for the purposes of this action, that Defendants received in excess of $100,000 in attorney's fees in each of the eight cases delineated in the Stipulation. *See* Aboulafia Affirm. Ex. D

("[Defendants] received attorneys fees in excess of $100,000 as a result of the resolution of [various] matter[s]").

2. *Not Subject to Usury Laws*

Second, Defendants argue that the Stipulation is a usurious loan that cannot be enforced. However, courts in similar cases have held that agreements nearly identical to the Sale Agreement and Stipulation are not loans and therefore are not subject to usury laws. *See Kelly Grossman & Flanagan, LLP v. Quick Cash, Inc.*, 35 Misc.3d 1205(A) (Sup. Ct. Suffolk Cnty. March 29, 2012) (holding advancement of money to fund lawsuit, and contingent right to receive attorneys' fees as repayment, was not loan subject to usury laws); *Lynx Strategies, LLC v. Ferreira*, 28 Misc.3d 1205(A) (Sup. Ct. N.Y. Cnty. July 6, 2010) (involving Defendant Jeffrey L. Lessoff and holding advancement of money to fund lawsuit, and contingent right to receive attorney's fees as repayment, was not loan subject to usury laws).

In *Lynx Strategies*, the court held that "usury applies to loans . . . [while] the instant transaction, by contrast, is an ownership interest in proceeds for a claim, contingent on the actual existence of any proceeds." *Lynx Strategies*, 28 Misc.3d 1205(A) at *2. As in the instant case, the *Lynx Strategies* court noted that "[h]ad respondent been unsuccessful in negotiating a settlement or winning a judgment,

petitioner would have no contractual right to payment." *Lynx Strategies*, 28 Misc.3d 1205(A) at *2.

The Sale Agreement states that "[Funding] desires to purchase a contingent interest in Proceeds . . . that may be recovered from any and all of the Claim(s)." *See* Aboulafia Affirm. Ex. C at 1. The use of the words "contingent" and "may" show that if there had been no recovery on the underlying actions, then Plaintiffs would not be entitled to any payment. Further, the Stipulation was not a loan, as no money passed from Plaintiffs to Defendants, but rather was a settlement of an underlying claim. Therefore, the Sale Agreement and the Stipulation are not loans, but investments, and are not subject to usury laws.

3. *No Improper Sharing of Attorney's Fees*

Defendants third argument against summary judgment is that the instant transactions constitute improper sharing of attorney's fees with a non-lawyer. The two New York cases involving lawsuit funding through the sale of an attorney's right to receive fees, while upholding the agreements, did not discuss ethical issues or potential violations of New York Rule of Professional Conduct 5.4(a).

However, courts in several other jurisdictions have addressed the interplay of alternative litigation financing and Rule 5.4(a). In *PNC Bank, Delaware v. Berg*, No.

94C-09-208-WTQ, 1997 WL 529978, at *10 (Del. Super. Ct. January 21, 1997), the court explained:

> The Tighe defendants suggest that it is "inappropriate" for a lender to have a security interest in an attorney's contract rights. Yet it is routine practice for lenders to take security interests in the contract rights of other business enterprises. A law firm is a business, albeit one infused with some measure of the public trust, and there is no valid reason why a law firm should be treated differently than an accounting firm or a construction firm. The Rules of Professional Conduct ensure that attorneys will zealously represent the interests of their clients, regardless of whether the fees the attorney generates from the contract through representation remain with the firm or must be used to satisfy a security interest. Parenthetically, the Court will note that there is no suggestion that it is inappropriate for a lender to have a security interest in an attorney's accounts receivable. It is, in fact, a common practice. Yet there is no real "ethical" difference whether the security interest is in contract rights (fees not yet earned) or accounts receivable (fees earned) in so far as Rule of Professional Conduct 5.4, the rule prohibiting the sharing of legal fees with a nonlawyer, is concerned. It does not seem to this Court that we can claim for our profession, under the guise of ethics, an insulation from creditors to which others are not entitled.
>
> *PNC Bank, Delaware*, at *10 n.5.

The *PNC Bank* decision has been quoted by the First Circuit, several federal district courts, and the Court of Appeals of Ohio. *See Cadle Co. v. Schlichtmann*, 267 F.3d 14, 18 (1st Cir. 2001) (upholding a security interest in a law firm's anticipated contingency fees); *Core Funding Grp., L.L.C. v. McDonald*, No. L-05-1291, 2006 WL 832833, at *11 (Ohio Ct. App. Mar. 31, 2006) (quoting *PNC Bank* and holding that "at this juncture, we cannot claim for appellees, under the guise of ethics, an insulation from

appellant-creditor"). *See also* ACF 2006 Corp. v. Merritt, No. CIV-12-161, 2013 WL 466603, at *3 n.1 (W.D. Ok. Feb. 7, 2013); *U.S. Claims, Inc. v. Yehuda Smolar, PC*, 602 F.Supp.2d 590, 597 (E.D. Pa. March 9, 2009); *U.S. Claims, Inc. v. Flomenhaft & Cannata, LLC*, 519 F.Supp.2d 515, 521 (E.D. Pa Nov. 13, 2006).

There is a proliferation of alternative litigation financing in the United States, partly due to the recognition that litigation funding allows lawsuits to be decided on their merits, and not based on which party has deeper pockets or stronger appetite for protracted litigation. *See* A.B.A. Comm. on Ethics 20/20, *Informational Report to the House of Delegates* 2 n.6 February 2012, *available at* http://www.americanbar.org/content/dam/aba/administrative/ethics_2020/20111212_ethics_20_20_alf_white_paper_final_hod_informational_report.authcheckdam.pdf; Sandra Stern, *Borrowing from Peter to Sue Paul: Legal & Ethical Issues in Financing a Commercial Lawsuit* ¶ 27.02[3] (2013). Therefore, this Court adopts the *PNC Bank* Court's reasoning and finds that the Stipulation does not violate Rule 5.4(a) and is not unenforceable as against public policy.

4. *Not Unconscionable*

Finally, Defendants contend that "[t]he amount of the loan, the terms, the fees, everything is unfair, unconscionable, not at arms length!" *See* Lessoff Affirm. ¶ 12. In

addition, Defendants argue that "the only thing [Plaintiffs] do not do is break your legs what do you call them." *See* Lessoff Affirm. ¶ 12.

"A determination of unconscionability generally requires a showing that the contract was both procedurally and substantively unconscionable, i.e., 'some showing of an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party.'" *Warburg, Pincus Equity Partners, L.P. v. Keane*, 22 A.D.3d 321, 322 (1st Dep't 2005) (quoting *Gillman v. Chase Manhattan Bank*, 73 N.Y.2d 1, 10 (1988)).

Defendants fail to carry their burden to show procedural and substantive unconscionability, or to raise an issue of fact precluding summary judgment. Defendants state that they "were desperate borrowers at the time of the loan, or else they would have received a much better rate," and that Defendants "had never not paid any debt, like this before. He has paid off any of these companies back." *See* Lessoff Affirm. ¶¶ 7, 8.

Defendants' conclusory assertions, without more, do not rise to the level of a procedurally and substantively unconscionable contract. "[A]n unconscionable contract has been defined as one which is so grossly unreasonable as to be unenforceable because of an absence of meaningful choice on the part of one of the parties together with contract terms which are unreasonably favorable to the other party." *King v. Fox*, 7 N.Y.3d 181, 191 (2006).

Here, Defendants received $108,500 to assist in prosecuting the delineated cases, with no guaranteed obligation to repay. Further, Defendants affirmed the allegedly "unconscionable" terms of the Sale Agreement by expanding upon the Sale Agreement's provisions in the Stipulation. Therefore, the agreements at issue here are not unconscionable.

Plaintiffs have established entitlement to summary judgment regarding Defendants' liability for breach of the Stipulation. Further, Defendants have failed to carry their burden to raise a genuine issue of material fact precluding entry of judgment.

VI. Damages

The single remaining issue to be determined is the amount of damages to which Plaintiffs are entitled under the Stipulation. The Stipulation contains multiple clauses defining Defendants' obligations to Plaintiffs, which will be considered in turn.

First, Section 2.2 of the Stipulation provides that Plaintiffs shall receive the attorneys fees that Defendants receive in eight named cases, up to an aggregate amount of $238,700. *See* Aboulafia Affirm. Ex. F at 2. Given that Defendants failed to timely respond to Plaintiffs' Notice to Admit, Defendants have admitted receiving in excess of $100,000 in attorney's fees in each of the eight cases defined in the Stipulation, or at least $800,000. *See* CPLR §3123(a); *Hernandez v. City of New York*, 95 A.D.3d 793, 794 (1st

Dep't 2012) ("Defendant is deemed to have admitted the facts contained in plaintiff's notice to admit, as it did not timely respond to the notice"). Therefore, Defendants are liable for the maximum amount of $238,700.

Second, Section 2.3 provides that Defendants must remit received fees within ten business days of receipt. *See* Aboulafia Affirm. Ex. F at 3. Further, Section 2.3 states that if Defendants fail to timely remit the fees, then the debt accrues interest at a rate of 3% per month, compounded monthly. There has been no evidence regarding when Defendants received legal fees in the eight cases. Therefore, further discovery is needed regarding this issue.

Third, Section 5 of the Stipulation provides for a penalty of $50 for each late payment made by Defendants under Section 2. *See* Aboulafia Affirm. Ex. F at 5. A payment is considered late fifteen days after Defendants' receipt of attorney's fees. *See* Aboulafia Affirm. Ex. F at 5. Therefore, each time Defendant's received attorneys fees subsequent to signing the Stipulation, and failed to remit that amount to Plaintiffs, a penalty of $50 should be assessed. This issue also requires further discovery regarding when fees were received by Defendants.

Fourth, Section 6.1(i) provides for $5,000 liquidated damages in the event Defendants default on the Stipulation. *See* Aboulafia Affirm. Ex. F at 5. As Defendants have defaulted on the Stipulation, Defendants are entitled to $5,000.

Finally, Section 6.2(ii) provides for full reimbursement of all reasonable legal and collections fees incurred due to Defendants' default. *See* Aboulafia Affirm. Ex. F at 5. The amount of attorneys and collection fees requires further discovery.

Defendants' remaining arguments have been considered and are not persuasive. Plaintiffs' other arguments are rendered moot.

CONCLUSION

Accordingly, it is hereby

ORDERED that Defendants' cross-motion for leave to amend the Answer is DENIED; and it is further

ORDERED that Defendants' cross-motion for summary judgment dismissing the Complaint is GRANTED in so far as it seeks to dismiss the first and second causes of action, and is otherwise DENIED; and it is further

ORDERED that the first and second causes of action are dismissed, the first and second causes of action are severed, and the Clerk is directed to enter judgement accordingly; and it is further

ORDERED that Plaintiffs' motion for partial summary judgment on the third and fourth causes of action is GRANTED as to liability; and it is further

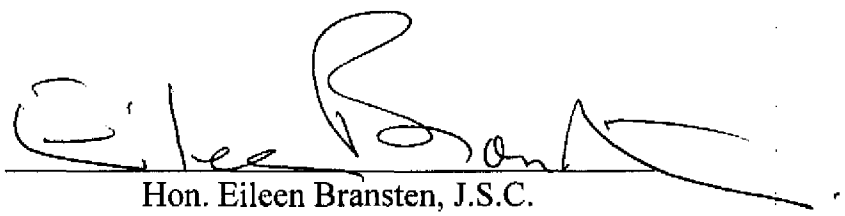
ORDERED that the branch of Plaintiffs's motion seeking additional discovery is GRANTED, and Plaintiffs are granted leave to serve additional disclosure demands on Defendants, within 30 days of the date of this Order, regarding the dates when Plaintiffs received legal fees in the eight cases listed in Section 2 of the Stipulation; and it is further

ORDERED that counsel for the parties are directed to appear for a status conference in Room 442, 60 Centre St, on Wednesday, February 5, 2014, at 10:45 a.m.

This constitutes the decision and order of the Court.

Dated: New York, New York
December 4, 2013

ENTER:



Hon. Eileen Bransten, J.S.C.

49 Rutgers L. Rec. 118

Rutgers Law Record
2022

Justin Boes [1]

LAWYERS, FUNDS, & MONEY: THE LEGALITY OF THIRD-PARTY LITIGATION FUNDING IN THE UNITED STATES

I. INTRODUCTION

Imagine there is a plaintiff with a meritorious claim, but, because of the high costs of litigation, he cannot afford to bring or maintain it. Though there is a market for such claims and feasible fee arrangements are available, his claim is nonetheless rejected because of the litigation costs, the high risk of losing, and/or the unlikelihood of settlement. The claim, regardless of its merits, is over before it begins. There is now, however, one more option available to such plaintiffs: third-party litigation funding.

Increasingly, third-parties--investors with no legal interests in cases--are funding lawsuits, bearing most or all of the cost and risk of litigation. [2] In exchange for financing a lawsuit, an investor will receive a large percentage of an award or settlement. [3] Third-party litigation funding's proponents believe it empowers claimants to bring meritorious claims against defendants, providing them the otherwise unobtainable sling and rocks needed to challenge corporate goliaths. [4] Its opponents--chief among them the U.S. Chamber Institute for Legal Reform, an affiliate of the U.S. Chamber of Commerce--believe it encourages and enables claimants to bring frivolous and abusive claims and have, accordingly, attempted to frustrate these funding arrangements. [5]

In 2009, the U.S. Chamber Institute, recognizing that "third-party funding governed in the United States by a patchwork of relatively weak laws, cases, rules, and regulations," issued a seminal report on third-party litigation funding, predicting that it would cause substantial litigation abuse and that, under the doctrines of champerty and maintenance, it must be prohibited. [6]

American courts, despite the Institute's arguments, have largely upheld these arrangements on public policy grounds, concluding, like Australian and English courts before them, that, whatever the potential for abuse, third-party litigation funding allows low-resourced claimants greater access to justice. [7] The U.S. Chamber Institute thus re-focused its attention on the issue of disclosure, arguing that financing agreements must be disclosed to defendants. [8] In the twelve years since the Report's publication, American courts have grappled with the ***119** Institute's arguments and have, by and large, rejected them, permitting third-party litigation funding and placing materials relating to these financing agreements beyond the scope of discovery. [9]

Part I of this Note provides a general overview of third-party litigation funding, from its modern origins in Australia and England to the litigation market as currently constituted in the United States. It concludes with a discussion of the U.S. Chamber Institute's 2009 Report, putting it in the political context of the tort-reform movement.

Part II reviews court opinions over the last decade that have considered the issue of whether the doctrines of champerty and maintenance necessarily bar third-party litigation funding in the United States, issues that were unlitigated when the Chamber Institute published its 2009 Report.

Part III reviews court opinions over the last decade concerning third-party litigation funding in the discovery context. In particular, whether financing agreements are generally "relevant" within the meaning of Federal Rule of Civil Procedure 26(a) as well as whether these agreements are protected under attorney-client privilege or the work-product doctrine.

Finally, Part IV briefly considers other developments regarding the disclosure of third-party litigation financing agreements. In particular, an Institute-sponsored proposal to add an additional fifth prong to Rule 26(a) to the Rules of Civil Procedure, which would require parties to disclose financing agreements to opposing parties "without awaiting a discovery request." [10]

II. THIRD-PARTY LITIGATION FUNDING, AN OVERVIEW

The phrase "third-party litigation funding" has multiple meanings. As used in this Note, the phrase means, simply, any arrangement in which a non-party, with no legal interest in a lawsuit, contracts with a litigant to bear the costs of litigation in exchange for a percentage of the reward.

A. Modern Origins

While these arrangements date to Ancient Greece and Rome, where funders' motivations were socio-political, not economic, [11] the development of modern third-party litigation funding, as now practiced in the United States, originates in Australia in the 1990s. [12] Though Australia--and other common-law countries, like the United Kingdom [13] --was historically hostile to third-party intermeddling in litigation, it gradually began to relax restrictions on these arrangements, allowing them in insolvency proceedings and, eventually, in civil litigation generally. [14] Because ***120** Australia severely limits the use of contingency fees, [15] its courts came to recognize that third-party litigation funding would allow claimants of more modest means greater access to justice. [16] Since Australia includes the winning party's attorneys' fees in any damages award (the so-called British rule), [17] its courts were likely convinced that third-party investors would be effectively deterred from funding meretricious litigation. Accordingly, the Australian government, recognizing the public policy potential of these arrangements, gradually loosened its centuries-old common-law prohibitions on third-party intermeddling, thereby creating a new market for legal claims and defenses. [18]

Australia's newly progressive attitude toward third-party involvement in litigation culminated with the High Court's 2006 decision in *Campbells Cash and Carry Pty. Ltd. v. Fostif Pty. Ltd.* [19] In *Fostif*, Firmstones & Feil, Consultants, a small, Sydney-based accounting firm, brought a representative action (the Australian equivalent of a **class** action) on behalf of 2,000 small tobacco retailers against sixteen tobacco companies, seeking to recover $100 million in licensing fees. [20] The accounting firm conceived of the claim, controlled the litigation, and, under the financing agreement, was due to receive one-third of the potential reward. [21] The companies argued that the agreement was clearly champertous and thus impermissible, but the High Court disagreed, finding that the arrangement was neither an abuse of process nor contrary to public policy. [22] In subsequent cases, the High Court clarified its ruling in *Fostif*, interpreting it to be "a ban on any general rule prohibiting the funding of litigation for reward." [23]

England, similarly, was re-evaluating its blanket bans on third-party intermeddling, abrogating all criminal and civil penalties for champerty in 1967. [24] In 2005, the English Court of Appeal clarified the uncertain legal status of litigation funding, holding in *Arkin* v. *Borchard Lines Ltd.* that litigation funding is not against public policy; on the contrary, it ruled that these arrangements facilitate access to justice, making them acceptable, provided the funder does not manage the litigation. [25]

With Australia and England legalizing third-party litigation funding, it seemed inevitable that the United States, another common-law country with high litigation costs, would likewise come to believe that this new form of third-party intermeddling should be permitted and promoted.

B. Defining Third-Party Litigation Funding

***121** The phrase refers both to the funding arrangement, as distinguished from contingency fees (when an "attorney advances services and other costs associated with prosecuting a case in exchange for a certain percentage of any recovery") [26] and litigation lending (when investors contract with a lawyer or the lawyer's firm, not the party in the lawsuit), [27] and the industry itself. [28]

In the simplest and most common funding arrangement, an investor--like a bank or **hedge fund** [29] --will fund a single case; in exchange, the investor will receive a percentage of the proceeds recovered from the case's resolution, whether through the courts or a settlement. [30] These are non-recourse arrangements, so, should the plaintiff lose, he is not obligated to recompense the investor. [31]

These arrangements, according to Victoria Shannon, in her article, *Harmonizing Third-Party Litigation Funding*, share two important characteristics: (1) the investor contracts directly with the client, not the client's lawyer, and (2) the investor never becomes a party to the lawsuit. [32] Aside from funding the lawsuit, the investor has no connection to the litigation.

C. The Litigation Finance Market

Over the last decade, third-party litigation funding has become a burgeoning, multibillion-dollar, international industry. [33] In the United States, third-party litigation funding has grown exponentially, with US-based commercial entities raising an estimated $1.8 billion in capital since 2016. [34] Burford Capital--a major, US-based litigation finance firm founded in 2009--reported spending over a billion dollars in investments in 2018, "the first time [it had] crossed that threshold." [35] While the majority of specialized funders are based in Australia, Germany, and the United Kingdom, where third-party litigation finance is more established, [36] there are increasingly more United States-based funders, which, like Burford, are devoted almost ***122** entirely to these investments. [37] These funders can be large, publicly-traded entities (like Burford Capital) or private funds (such as Longford Capital). [38]

There are two distinct litigation markets in the United States: commercial and consumer. [39] The commercial market typically concerns business-to-business disputes, such as anti-trust violations, intellectual property infringement, and trade secret misappropriation. [40] These cases can yield substantial rewards, exceeding $10 million. [41] The consumer market, by contrast, largely consists of personal injury claims. [42] These claims can are brought individually or as class actions, and, compared to commercial claims, yield smaller rewards. [43] While the paradigmatic client is an impecunious plaintiff who, without litigation funding, cannot afford to bring a claim, clients are increasingly varied, from pro bono legal services to Fortune 500 companies. [44]

Typically, a third-party investor is contacted after a lawsuit has been initiated. [45] The person bringing the claim or defending against it will provide the investor with limited information. [46] Using this information, the investor, like a risk analyst, will consider the strengths and weaknesses of the client's case, the likelihood of success, and the ability to actually recover. [47] Based on these perceived odds, the investor may contribute the capital necessary to maintain the lawsuit, usually on a non-recourse basis. [48]

Though litigation finance is a seemingly novel means of maintaining lawsuits, it is not so dissimilar from two more-established legal lending schemes. As Jason Lyon observes in his article, *Revolution in Progress: Third-Party Funding of American Litigation*, the basic third-party litigation agreement (an outside investor bearing litigation costs on a non-recourse basis) is comparable to pre-settlement funding and syndicated lawsuits. [49] Under a pre-settlement agreement, an investor covers a litigant's living expenses while a lawsuit is pending, which are secured against a potential reward or settlement. In syndicated lawsuits, litigants, as a means of funding their lawsuits, sell partial rights in any reward or settlement to private investors; these investors, in turn, sell shares in the lawsuits. [50] The crucial difference between these schemes and third-party litigation funding is the size of the investment, and, concomitantly, the size of a ***123** potential award. [51] Whereas the average pre-settlement loan a decade ago was no greater than $20,000, third-party investments often exceed $15 million, with potential awards of $100 million, [52] figures that have only increased over the intervening eleven years. [53]

D. A Recipe for Abuse | The U.S. Chamber Institute for Legal Reform's 2009 Report

It was, one imagines, the predicted increase in mass torts, caused by third-party litigation funding, and the mammoth size of potential awards that inspired the U.S. Chamber Institute for Legal Reform to issue a report in October 2009 lambasting the practice. [54] While other defendant-and business-favoring organizations, like the American Tort Reform Association, likewise issued papers criticizing alternative litigation financing around the same period, [55] the Institute's 2009 Report became the "landmark piece for all criticism of the practice." [56]

The Report, prepared by attorneys from Skadden, Arps, Slate, Meagher & Flom, [57] was written after two major victories for the so-called tort reform movement. In 2005, President George W. Bush signed the Class Action Fairness Act ("CAFA"), which changed subject-matter jurisdiction rules governing class action lawsuits, allowing them to be removed from more plaintiff-friendly state courts to more defendant-favoring federal courts. [58] The ostensible purpose of the Act was to curb class action abuse, though opponents believe Congress' true motivation was to minimize corporate liability. [59] In 2007, in *Bell Atlantic Corp. v. Twombly*, the United States Supreme Court adopted a new pleading standard for federal complaints, supplanting the plaintiff-favoring notice pleading standard from *Conley v. Gibson* with a new, defendant-favoring plausibility standard, requiring plaintiffs to now demonstrate, "through factual matter," a "plausible" claim for relief. [60] Together, the Class Action Fairness Act and new "plausibility" pleading standard created greater hindrances for claimants, particularly in the class action context. The Act forced plaintiffs filing class action claims into less sympathetic federal courts, while the *Twombly* plausibility standard effectively made the barrier to entry higher for plaintiffs, further insulating defendants (especially businesses) from large lawsuits. Third-party litigation funding, then-fast developing in Australia and Europe, threatened to undermine these legislative and judicial victories.

With third-party litigation funding's legal status unclear, the U.S. Chamber Institute issued its 2009 Report with the goal of persuading courts and legislatures to revive the almost obsolete torts of champerty and maintenance, thus making third-party litigation illegal in the ***124** United States. [61] The Chamber's fear, one speculates, was that American courts, like the common-law courts of Australia and England, would similarly find the medieval rationales for these torts uncompelling. Worse, American courts would not only permit such financing, they would promote it on public policy grounds, seeing these financing arrangements, like the courts in *Fostif* and *Arkin*, as a commendable means of promoting greater access to justice for indigent plaintiffs. A report from a well-known lobbying group on a little-known subject, framed in terms favorable to the organization's objectives, could have an agenda-setting effect, persuading courts and legislatures--primed, after CAFA and *Twombly*, to be wary of aggregate litigation--that the potential for frivolous and abusive lawsuits, enabled by third-party litigation funding, would far outweigh whatever access to courts such financing might provide.

Under the existing contingency-fee based system, the Report argues, only meritorious claims are brought, as this system, combined with the high cost of litigation, disincentivizes attorneys working on contingency from bringing non-meritorious claims. [62] Because third-party litigation funding allows attorneys to "offload" the cost and risk of litigation, frivolous and abusive cases "that plaintiffs and their attorneys ordinarily would not have pursued are [now] much more likely to be filed." [63] This risk of abusive litigation is especially pronounced in the class action context, which, the Report notes, was "already very vulnerable to abuse." [64]

Using the familiar David and Goliath analogy, the Report reverses the roles. [65] The victims of this anticipated increase in abusive aggregate litigation would not be corporate goliaths. [66] It would be motorists, professional-service providers, and small-business owners, people and entities who cannot financially contend with investor-backed classes and, accordingly, will face coercive pressure to settle cases, regardless of the merits, as that would be the more economically efficient option for them. [67] However, the Report optimistically concludes, this future of unbridled frivolous litigation is not inevitable. [68] In 2009, when the Report was published, third-party funding was not prevalent and "governed by 'a patchwork of relatively weak laws, cases, rules, and regulations--and they are only in force in a handful of states.'" [69] The United States could thus avoid the fates of Australia and Europe by prohibiting the practice entirely or, at a minimum, prohibiting its use in aggregate litigation. [70]

III. CHAMPERTY & MAINTENANCE AS APPLIED TO THIRD-PARTY LITIGATION FUNDING IN THE UNITED STATES

A. Historical Background

***125** In its 2009 Report, the U.S. Chamber Institute complained that there was no nationwide consensus or conversation regarding the continued viability of champerty and maintenance and whether these doctrines would bar third-party litigation funding. [71] While courts had not yet applied them to litigation finance, discussion of champerty and maintenance, contrary to the Institute, had been ongoing since the founding of the United States. [72]

Beginning in the nineteenth-century, as public attitudes towards third-party involvement in litigation were slowly changing, American courts started to question the extent to which these torts should be enforced to prevent third-party intervention. [73] Though American courts were increasingly sympathetic to indigent plaintiffs, who, despite having legitimate claims, lacked the financial means to file suit, courts were also wary of money-minded third-parties, who, they feared, would intermeddle in litigation solely for profit. As then-Judge Cardozo, writing for the New York Court of Appeals in 1929, succinctly put it: "[I]t seems to be agreed that anyone may lawfully give money to a poor man to enable him to carry on his suit .... What is feared and forbidden is the oppressive intermeddling of wealth or officialdom for publicity or profit." [74]

Over the twentieth-century, with the advent of Legal Aid, the public increasingly supported limiting the enforcement of champerty and maintenance to allow indigent claimants greater access to courts, but these torts were not all together eliminated. [75] The tort of maintenance continued to prevent attorneys from soliciting clients, and the tort of champerty continued to prevent attorneys from working on contingency. [76] Third-party litigation funding thus presented a thorny problem, as it both supported the public interest's in providing indigent claimants greater court access while, at the same time, risked allowing third-parties to profit from those claimants' lawsuits. In 1998, when European firms started to fund lawsuits in the United States, [77] it was an open question whether the public interest would overcome these for-profit concerns. During the last decade, some states, discussed *infra*, have found that the risk of profiteering outweighs the purported benefits of providing indigent claimants greater access to courts and, accordingly, have prohibited third-party funding of claims. The general trend, however, is to allow such arrangements.

B. *Case Study* | Minnesota's Prohibition on Third-Party Litigation Funding

Third-party litigation funding's opponents argue that these funding arrangements constituted champerty and/or maintenance, making them illegal. [78] Champerty, a common-law tort under English law, is an agreement "between a stranger to a lawsuit and a litigant by which the stranger pursues the litigant['s] claims as consideration for receiving part of any judgment ***126** proceeds." [79] Maintenance, a similar concept, is the assistance in "prosecuting or defending a lawsuit given to a litigant by someone who has no bona fide interest in the case; meddling in someone else's litigation." [80] The U.S. Chamber Institute's 2009 Report expressly argued that these common-law torts bar third-party litigation funding. [81] A decade after its publication, courts have now ruled on the legality of these funding arrangements and some, like the Institute, agree that these torts render third-party financing impermissible.

Minnesota, for example, in *Maslowski v. Prospect Funding Partners LLC*, refused to exempt litigation funding arrangements from its champerty and maintenance doctrines, effectively banning such arrangements in the state. [82] In 2012, the plaintiff sued to recover damages for injuries sustained in an automobile accident. [83] While her suit was pending, the plaintiff entered into a non-recourse agreement with the defendant, a litigation funder. [84] In exchange for giving the plaintiff $6,000, which she needed for living expenses, the defendant was promised $6,000, a $1,425 processing fee, and 60 percent annual interest from a potential award. [85] After winning her case, the plaintiff brought suit against the defendant, seeking a declaratory judgment that their contract was champertous and thus unenforceable. [86]

The Minnesota Court of Appeals, finding for the plaintiff, ruled that, while other states have eschewed or changed their doctrines to allow for litigation funding, Minnesota would continue to "follow [its] common-law rule prohibiting contracts

for champerty." [87] These contracts, the court concluded, agreeing with and quoting the lower court's opinion, implicated several public policy concerns--in particular, disincentivizing settlement. [88] "[U]nless the amount recovered would exceed ... the amount [plaintiff] would owe to the litigation funding company," she has no incentive to settle. [89] The more a plaintiff owes, the greater her unwillingness to settle, making litigation longer and costlier. [90]

Here, the Minnesota Court of Appeals portends what would later become a central argument against third-party litigation funding and the related need for disclosure: disincentivizing settlement. Without knowing the particulars of a contract or with whom the defendant is actually negotiating, the parties cannot settle cases, something the courts encourage. This inability to settle cases makes them longer, costlier, and ensures they are not decided on the merits. Minnesota is not alone is outlawing or limiting third-party litigation funding; five other states, including Pennsylvania, have explicitly applied these doctrines to litigation funding. [91]

*127 C. *Case Study* | Illinois & the Legality Third-Party Litigation Financing

Maslowski and these states notwithstanding, courts are trending toward limiting the doctrines of champerty and maintenance to allow for third-party litigation funding. [92] As American courts declined to extend these doctrines to contingency fees (finding a public policy interest in "supporting access to justice by means of contingency fees"), [93] twelve states, including New Jersey, either no longer recognize these doctrines or have excepted litigation funding from them. [94]

For instance, in *Miller UK Ltd. v. Caterpillar, Inc.*--a case that concerns both champerty and maintenance as well as the "relevance" of third-party investors for discovery purposes--the United States District Court for the Northern District of Illinois ruled that a litigation funding agreement did not constitute maintenance, making the structure and terms of the arrangement irrelevant and thus undiscoverable. [95]

In 2010, after a multi-decade busines relationship, Miller brought suit against Caterpillar, alleging misappropriation of trade secrets. [96] Caterpillar, the better-resourced of the parties, used "scorched earth" tactics to overwhelm its opposition, prolonging discovery disputes in an effort to pressure Miller to "abandon the case or settle on distinctly disadvantageous terms." [97] Miller, resisting this pressure, contracted with a third-party litigation funder, bolstering its financial position. [98] Caterpillar moved to compel production of the funding contract, arguing that it constituted maintenance, making its contents relevant. [99]

The district court was unconvinced, finding that the contract was not a form of maintenance. [100] In Illinois, a person is guilty of maintenance when he "officiously intermeddles" in a lawsuit that neither belongs to nor concerns him. [101] In other words, a person who provides unsolicited financial support for a lawsuit, despite having no bona fide legal interest in it, is guilty of this "hoary" doctrine. [102] Here, though, the funder's assistance was not unsolicited. [103] "The funder was sought out by a cash-strapped litigant embroiled in bitterly contested litigation," and the lawsuit itself, which Miller initiated, was not intended to promote a meritless cause. [104] "The funders were sought out by Miller to enable it to continue with the litigation that Miller had initiated in 2010 without prompting from any funder." [105] Because Caterpillar could not sustain a defense of maintenance, the contract and other "deal documents" were irrelevant under 26(b)(1) ***128** of the Rules of Federal Procedure. [106] The court, accordingly, denied the defendant's motion to compel. [107]

IV. THIRD-PARTY LITIGATION IN THE DISCOVERY CONTEXT

A. The Relevance of Third-Party Litigation Funding Agreements Within the Meaning of Federal Rule of Civil Procedure 26(b)(1)

As with champerty and maintenance, courts also disagree about whether, when, and to what extent third-party litigation funding agreements are "relevant" within the meaning of Rule 26(b)(1) and thus discoverable. [108]

Rule 26(b)(1) sets the scope of federal discovery. [109] The parties can obtain information that is relevant to their claims or defenses, provided the information is proportional to the needs of the case and is not work-product or privileged. [110] This rule, according to the Supreme Court, should "be accorded a broad and liberal treatment to effect [its] purpose of adequately informing the litigants in civil trials." [111] However, the courts, in controlling the discovery process, must be mindful of Rule 1, which commands that civil trials be "just, speedy, and inexpensive." [112] Rule 26(b)(1)'s relevancy requirement should, therefore, be "firmly applied," and courts should not hesitate to use their power to protect parties from "annoyance, embarrassment, oppression, or undue burden or expense" as required under Rule 26(c)(1)(A). [113]

1. *Case Study* | West Virginia and the Relevance of Financing Agreements

In a relatively early example of a court finding litigation funding arrangements relevant, the United States District Court for the Southern District of West Virginia took a broad view of relevance. [114] In *American Medical Systems*--the infamous pelvic mesh case, which the U.S. Chamber Institute highlights as an egregious example of third-party litigation funding and the urgent need for disclosure--the court refused to grant a protective order, allowing documents "related to the referral, transfer, or sale of [the] litigation claims to law firms" to be subpoenaed. [115]

American Medical Systems addressed a discovery dispute stemming from a mass tort, multidistrict litigation concerning the manufacture and marketing of allegedly defective pelvic mesh products. Because the mesh, "used to correct a condition called pelvic organ prolapse," was allegedly defective, plaintiffs were required to undergo corrective surgeries to revise or ***129** remove them. [116] It was later revealed, as reported in the *New York Times*, that some of these surgeries were medically unnecessary, with third-party funders "coaxing women into having surgery" in order to increase the recovery in "lawsuits against medical device manufacturers." [117]

During discovery, AMS learned that these surgeries were "arranged and funded through third-party funding companies," raising questions about the necessity of the surgeries. [118] With plaintiffs refusing to disclose the details of these funding arrangements, AMS subpoenaed two nonparties, demanding documents "pertaining to ownership or financial interest in ... [the] funding companies." [119] These nonparties also refused, arguing that the information was irrelevant because "it relates to 'suspected wrongdoing' of the nonparties rather than the claims and defenses in this litigation." [120] In response, AMS argued that, because the information "related to the plaintiffs' decisions to undergo corrective surgeries," it was "relevant to the reasonableness and medical necessity of [said] surgeries." [121]

The court, after noting previous discovery disputes and what AMS was and was not entitled to, found that most of the demanded documents were relevant to the litigation. [122]

> The subpoenas do not evidence a crusade against the nonparties' business practice; instead, AMS reasonably seeks to understand the motivation behind the plaintiffs' decisions to undergo corrective surgeries and how those surgeries were funded. A rational place to start is with the beginning of the money trail--the first entity interacting with the plaintiffs before the decision to have a corrective surgery is made. [123]

While the court did find the litigation funders and funding arrangement relevant, the particulars of the case, not a bright-line rule, resolved the discovery dispute. The case is more notable for its analysis of "relevance" within the meaning of Rule 26. The court concluded that, despite recent changes to the language of the rule and a new emphasis on proportionality, relevance, for discovery purposes, is broad and should be liberally construed, setting a standard that most parties can easily satisfy. [124]

2. *Case Studies* | New Jersey, Illinois, and the Irrelevance of Litigation Financing Agreements

The United States District Court of New Jersey, by contrast, recently held that funding agreements are not relevant, dismissing defendants' arguments as "pure speculation." [125] In ***130** *Valsartan*, another multidistrict litigation, mass tort case, plaintiffs

alleged a generic drug used to treat high blood pressure contained carcinogens, causing personal injuries and economic loss. [126] In pre-discovery discussions, defendants requested "all documents and communications related to funding or financing, if any, you or your counsel have obtained to pursue this litigation." [127] Plaintiff refused, arguing their "private financial information is irrelevant to [defendants] claims and defenses ...". [128]

The court, acknowledging that "courts are split," [129] agreed with plaintiffs that defendants demonstrated "no legitimate need for the requested information." [130] Unless defendants can actually show an alleged agreement's relevance, the court will not direct "carte blanche discovery of plaintiffs' litigation funding ...". [131] While defendants posited a parade of horrible scenarios that could arise from funding agreements, mere suggestions, without substantiation, did not make the agreements relevant. [132] "The fact that defendants have raised no nonspeculative basis for their discovery request results in its denial." [133]

Not all litigation funding concerns multidistrict litigation mass torts. In *Fulton* v. *Foley*, a plaintiff sued the City of Chicago, alleging he was wrongfully charged and convicted of sexual assault and murder, resulting in an almost twenty-five year prison sentence. [134] Chicago subpoenaed non-party Momentum Funding, LLC, whom it suspected of funding plaintiff's lawsuit, and demanded documents related to "all funding agreements and statements of the terms of funding." [135] Plaintiff moved to quash, arguing the information was not relevant within the meaning of Rule 26(b)(1). [136]

The court, acknowledging a plethora of decisions finding similar documents irrelevant, averred that questions of relevance must be decided on a case-by-case basis, with due consideration being given to the parties' arguments. [137] Yet, like in the other cited cases, defendants failed to persuade the court. [138] Like in *Maslowski*, the defendant argued that, without knowing the terms of the litigation agreement, it could not engage in settlement discussions. The court reminded the defendant that the standard for relevance is whether the evidence relates to the party's claims or defenses. [139] "Even if the documents could somehow be relevant for settlement discussions, settlement considerations are a wholly distinct concept and not a proper basis to obtain discovery under Rule 26(b)(1)." [140]

***131** The defendant also argued that the documents were somehow relevant to plaintiff's bias. [141] This argument also failed to satisfy the relevance standard. [142] "The assistance of litigation funding, in order to pay the fees and expenses of a litigation, does not assist the fact-finder in determining the credibility of plaintiff's testimony. Rather, the mere fact that plaintiff stands to gain from a successful lawsuit (with or without litigation funding) is the relevant inquiry on cross-examination concerning bias. Litigation funding does not change or add to the nature of that inquiry." [143] Accordingly, defendant's subpoena was quashed, concealing the details of the agreement. [144]

B. Attorney-Client Privilege & Work-Product As Applied to Third-Party Litigation Funding

Assuming that financing agreements are relevant within the meaning of Rule 26(b), these agreements might nonetheless be privileged or work-product protected, making them undiscoverable.

1. *Case Study* | Illinois & the Waiver of Attorney-Client Privilege

When a litigant solicits third-party funding, the litigant often provides the potential investor with limited information, allowing the investor to better assess the strengths and weaknesses of the case. [145] Proponents of disclosure argue that, in sharing this information, litigants waive their attorney-client privilege, so, pre-supposing the information is relevant within the meaning of the Rule 26(b), the details of these financing agreements must be disclosed upon request. Here, too, there is no national consensus, but of the courts who have considered the issue, a majority have found that, in disclosing information to potential investors, litigants waive their attorney-client privilege as to that information. [146]

In *Miller*, for example, the United States District Court for the Northern District of Illinois found that, in sharing information with a third-party investor, the plaintiff waived its attorney-client privilege as to that information. [147] The court noted that the

purpose of attorney-client privilege is to ensure confidentiality. [148] While documents pertaining to legal advice on business matters can fall under this privilege, [149] when such documents are prepared with the intent of sharing that information with an unprotected third-party, that information is no longer confidential and, thus, the privilege is waived. [150] The court also held that the common defense exception--which allows disclosure of confidential communications to third-parties, provided ***132** those parties share a common legal interest with the client--did not apply. [151] Because the third-party funder had a commercial interest, not a legal one, the exception could not be asserted. [152]

2. *Case Study* | Texas & the Protection of Financing Agreements and Related Materials Under the Work-Product Doctrine

Similarly, proponents of disclosure argue that, in sharing information with potential investors, litigants also waive their work-product protection as to that information. Here, though, courts are generally trending toward finding these materials protected and thus undiscoverable. [153]

For example, in *Mondis Technology, Ltd. v. LG Electronics., Inc.*, the United States District Court for the Eastern District of Texas held that the work-product doctrine extends to materials created to solicit third-party litigation funding. [154] In *Mondis*, the plaintiff, with the assistance of its counsel, prepared presentations for potential investors, including documents relating to its litigation strategy. [155] The defendant moved to compel production of these documents, but the plaintiff refused, asserting the documents were work-product protected and thus undiscoverable. [156] Unlike the attorney-client privilege, the mere disclosure of work-product to third-parties does not waive the protection; the protection is waived "only if work-product is given to adversaries or treated in a manner than substantially increases the likelihood that an adversary will come into possession of the material." [157] Because the disclosure of these documents to third-parties did not substantially increase the likelihood that the defendant would come into possession of them, the protection was not waived and the presentations were thus undiscoverable. [158]

V. RELEVANT DEVELOPMENTS: RULES CHANGES, COURT RULES, & LEGISLATION, PROPOSED AND PASSED

A. Advisory Rules Committee

Instead of litigating whether investors' identities are relevant and thus discoverable under 26(b), a coalition of business organizations have proposed amending Rule 26 to require "disclosure of third-party litigation funding arrangements in any civil action filed in federal court." [159] In 2014 and 2016, the Advisory Committee on Rules of Civil Procedure twice declined to adopt the above-proposal, concluding that such action would be "premature," given the ***133** nascent nature of the issue. [160] In 2017, despite these rejections, the coalition submitted another proposal: an additional fifth prong (26(a)(1)(A)(v)), under which all parties would have to provide:

> [F]or inspection and copying under Rule 34, any agreement under which any person, other than an attorney permitted to charge a contingent fee representing a party, has the right to receive compensation that is contingent on, and sourced from, any proceeds of the civil action, by settlement, judgment, or otherwise. [161]

The amendment-process is difficult, and, since opinions on third-party litigation funding seem to fall along the liberal-conservative divide, adoption of the amendment is not guaranteed. [162] The process is as follows. First, all proposed amendments to the Rules are sent to the Advisory Committee, which responds to these proposals in an Agenda Book. [163] If the Advisory Committee recommends one of the proposed amendments, the recommendation is forwarded to the Judicial Conference, the policy-making body for the federal judiciary, composed of Article III judges. [164] If approved by the Judicial Conference, the proposed amendment is forwarded to the Supreme Court, which, by majority vote, can approve the amendment. [165] The

Supreme Court has until May 1 to vote on amendments. [166] Finally, if the Supreme Court approves an amendment, it is forwarded to Congress, which can reject the amendment up until December 1. [167]

While the Advisory Committee on Rules of Civil Procedure has not officially rejected the proposal, statements from sub-committees indicate that this, too, will not be adopted. For instance, in 2019, the MDL Subcommittee of the Advisory Committee on Rules of Civil Procedure noted that, as of now, it is unwilling to adopt a rule addressing third-party disclosure:

> The MDL Subcommittee continues to study third-party litigation funding (TPLF), including various proposals for disclosure. All that is clear at the moment is that the underlying phenomena that might be characterized as third-party funding are highly variable and often complex. They continue to evolve at a rapid pace as large third-party funders expand dramatically. It seems clear that more study will be required to determine whether a useful disclosure rule could be developed. Nor does it seem likely that the several advisory committees will soon be in a position ***134** to frame possible expansions of disclosure requirements designed to support better-informed recusal decisions. [168]

B. The Litigation Funding Transparency Act

Assuming the Rules are not amended, the easier means of mandating disclosure is through the legislature. It should be noted, of course, that while passing a law is easier than amending the Rules, laws are easier to repeal, making a Rules-change the more attractive option to third-party litigation funding's opponents. In 2019, Senator Chuck Grassley, then-Senate Judiciary Committee Chair, introduced the above-named act, the express purpose of which was to make mandatory the disclosure of an investor's identity to both the court and "all other named parties" in class action suits. [169] An identical bill was introduced in March 2021. [170] The law, argued Senator Ben Sasse, echoing the language of Rule 1, would ensure that decisions are premised on laws and facts, not "the size of your bank account". [171] "By shedding light on funding arrangements, this legislation is a common-sense step toward making transparency the rule." [172]

C. West Virginia, Wisconsin, 7 & the Northern District of California

Some states have begun to regulate third-party litigation funding, including requiring disclosure of funders. For instance, in 2018, Wisconsin--using the above-quoted language from the U.S. Chamber Institute for Legal Reform's proposed amendment--changed its discovery laws, requiring that all funding agreements be disclosed "without awaiting a discovery request." [173]

In 2019, West Virginia, following Wisconsin's example, also required disclosure of what it terms "litigation financing contracts." [174]

In 2017, the Northern District of California adopted a rule requiring automatic disclosure of third-party litigation funding in class action lawsuits, the first such rule in the nation. [175] The revised rules now requires that, in any proposed class, collective, or representative action, the required disclosure includes any person or entity that is funding the prosecution of any claim or ***135** counterclaim. [176] Similarly, in June 2021, the U.S. District Court for the District of New Jersey amended Rule 7.1.1 of its Local Civil Rules. [177] Now, parties using third-party litigation financing must disclose the existence of "any person or entity that is not a party and is providing funding for some or all of the attorneys' fees and expenses for the litigation on a non-recourse basis." [178]

VI. CONCLUSION

In conclusion, American courts, despite the U.S. Chamber Institute's 2009 Report, have generally refused to extend the medieval doctrines of champerty and maintenance to prohibit third-party litigation funding in the United States, concluding, like the common-law courts in Australia and England, that, whatever their potential for abuse, these financing arrangements will allow

low-resourced claimants greater access to justice. While debates regarding disclosure of these agreements are ongoing, third-party litigation funding is now, indisputably, an unabrogable part of civil litigation in the United States.

Footnotes

1 J.D. Candidate, Rutgers Law School, Class of 2022; Senior Articles Editor, *Rutgers Law Record*.

2 Victoria A. Shannon, *Harmonizing Third-Party Litigation Funding*, 36 CARDOZO L. REV. 861, 863 (2015).

3 *Id.*

4 *See* Joseph J. Stroble & Laura Welikson, *Third-Party Litigation Funding: A Review of Recent Industry Developments*, 87 DEF. COUNS. J. 1, 2 (2020).

5 *See generally* John Beisner et al., U.S. Chamber Inst. For Legal Reform, Selling More Lawsuits, Buying More Trouble: Third-Party Litigation Funding a Decade Later (2020) [hereinafter Chamber Report II].

6 John Beisner et al., U.S. Chamber Inst. For Legal Reform, Selling Lawsuits, Buying Trouble: Third-Party Litigation Funding in the United States (2009) [hereinafter Chamber Report I].

7 *See* Stroble & Welikson, *supra* note 4, at 7.

8 Chamber Report II, *supra* note 5, at 26.A

9 *See* Stroble & Welikson, *supra* note 4, at 10-15.

10 Fed. R. Civ. P. 26(a).

11 *See* Gina Marco Solas, Third Party Litigation Funding: A Comparative Analysis 15 (2017) (Ph.D. thesis, University of Cagliari).

12 Maya Steinitz, *Whose Claim Is This Anyway? Third-Party Litigation* Funding, 95 MINN. L. REV. 1268, 1279 (2011).

13 *See* Solas, *supra* note 11, at 22-25.

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15 *Id.* at 1278 n.23.

16 *Id.* at 1279.

17 *Id.* at 1278 n.23.

18 *Id.* at 1279.

19 *Campbells Cash and Carry Pty. Ltd. v. Fostif Pty. Ltd.* [2006] 229 CLR 386 (Austl.).

20 Marcus Priest, *Retailers Fight Tobacco Firms Over Fees*, FINANCIAL REVIEW (Sept. 9, 2003, 10:00 AM), https://www.afr.com/policy/health-and-education/retailers-fight-tobacco-firms-over-fees-20030909-jv0*o*2.

21 *Campbells Cash and Carry Pty. Ltd. v. Fostif Pty. Ltd.* [2006] 229 CLR 386 (Austl.).

22 *Id.*

23 *See* Steinitz, *supra* note 12, at 1280.

24 *Id.*

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26 Jason Lyon, *Revolution in Progress: Third-Party Funding of American Litigation*, 58 UCLA L. REV. 571, 574 (2010).

27 *See* Shannon, *supra* note 2, at 863 n.3.

28 *See* Steinitz, *supra* note 12, at 1275-77.

29 *See* Shannon, *supra* note 2, at 871.

30 *See* Lyon, *supra* note 26, at 577.

31 *Id.*

32 Shannon, *supra* note 2, at 863 n.3.

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35 BURFORD CAP., BURFORD CAP. ANN. REP. 2019 (2019), https://www.burfordcapital.com/media/1734/fy-2019-report.pdf.

36 *See* Shannon, *supra* note 2, at 872.

37 *See* Letter from Laws. for Civ. Just. & U.S. Chamber Inst. for Legal Reform to Rebecca A. Womeldorf, Sec. of the Comm. on Rules of Prac. & Proc. of the Admin. Off. of the U.S. Cts., December 21, 2020, Appendix B, https://www.lfcj.com/uploads/1/1/2/0/112061707/lcj_and_ilr_letter_on_tplf_to_civil_rules_committee_dec_21_2020.pdf.

38 *See* Thompson, *supra* note 34.

39 *Id.*

40 *Id.*

41 *Id.*

42 *Id.*

43 *Id.*

44 *Id.* at 218.

45 *See* Shannon, *supra* note 2, at 872.

46 *Id.*

47 *Id.*

48 *Id.*

49 *See* Lyon, *supra* note 26, at 574.

50 Ari Dobner, *Litigation For Sale*, 144, U. PA. L. REV. 1529, 1529 (1996).

51 *See* Lyon, *supra* note 26 at 574.

52 *Id.*

53 *See* Thompson, *supra* note 34.

54 Chamber Report II, *supra* note 5.

55 *See* Letter from the Am. Tort Reform Ass'n, to Philip H. Schaeffer & Jeffrey B. Golden, Co-Chairs of the Am. Bar Ass'n Working Group on Alternative Litigation Financing (Feb. 15, 2011).

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58 28 U.S.C. § 1332(d) (2012).

59 Jeffrey L. Roether, *Interpreting Congressional Silence: Cafa's Jurisdictional Burden of Proof in Post-Removal Remand Proceedings*, 75 FORDHAM L. REV. 2745, 2752 (2007).

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64 *Id.* at 1.

65 *Id.* at 4.

66 *Id.*

67 *Id.* at 4, 7.

68 *Id.* at 12.

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70 *Id.* at 12.

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72 *See* Lyon, *supra* note 26, at 581.

73 *Id.* at 581-82.

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76 *See* Lyon, *supra* note 26, at 582.

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83 *Id.*

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85 *Id.*

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87 *Id.* at 763.

88 *Id.*

89 *Id.*

90 *Id.*.

91 *See* Thompson, *supra* note 34, at 220.

92 *See* Stroble & Welikson, *supra* note 4, at 7.

93 *See* Solas, *supra* note 11, at 29.

94 *See* Thompson, *supra* note 34, at 220.

95 Miller UK Ltd. v. Caterpillar, Inc., 17 F. Supp. 3d 711, 728 (N.D. Ill. 2014).

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97 *Id.* at 718.

98 *Id.* at 719.

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101 *Id.* at 725.

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104 *Id.* at 725.

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127 *Id.* at 614.

128 *Id.*

129 *Id.*

130 *Id.*

131 *Id.* at 619.

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139 *Id.* at *3.

140 *Id.*

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145 *See* Shannon, *supra* note 2, at 872.

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148 *Id.* at 731.

149 *Id.* at 730.

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153 *See* Stroble & Welikson, *supra* note 4, at 1513.

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158 *Id.* at *3.

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169 Litigation Funding Transparency Act, S. 471 116th Cong. (2019).

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49 RULREC 118

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United States District Court, N.D. Iowa, Western Division.

Anthony NUNES, Jr., Anthony Nunes, III, and NuStar Farms, LLC, Plaintiffs,
v.
Ryan LIZZA and Hearst Magazine Media, Inc., Defendants.

No. 20-cv-4003-CJW
|
Signed 10/26/2021

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ORDER REGARDING DEFENDANTS' MOTION TO COMPEL THIRD-PARTY FUNDING DISCOVERY REQUESTS

Mark A. Roberts, United States Magistrate Judge

***1** Before me is Defendants' Resisted Motion to Compel Responses to Third-Party Litigation Funding Discovery Requests, filed on August 23, 2021. (Doc. 147.) Plaintiffs filed a timely resistance. (Doc. 153.) Defendants filed a reply. (Doc. 157.) On September 14, 2021, I held a telephonic hearing and heard arguments from the parties. (Doc. 161.)

I. BACKGROUND

Plaintiffs operate a dairy in northwest Iowa. The individual Plaintiffs are close family members of prominent United States Congressman Devin Nunes. The claims arise out of an alleged defamatory article written and published by Defendants. The only remaining allegation is that Defendants defamed Plaintiffs because the article accused them of knowingly employing undocumented laborers. (Doc. 50.)

Defendants seek to obtain information about third parties whom they believe are funding this case for Plaintiffs. Specifically, Defendants have propounded request for production no. 92 that seeks:

> Documents sufficient to show the person or persons who, or entity or entities that, are funding Plaintiffs' prosecution of this action, including but not limited to the person or persons who, or entity of entities that, are paying Mr. Biss's and/or Mr. Feller's legal fees.

(Doc. 148 at 2.) [1] Plaintiffs' response to the request merely objected on relevance grounds. Defendants point to evidence that Plaintiffs are not, in fact, paying for the instant litigation. That is, they have not incurred out-of-pocket expenses and have made only a minimal payment to local counsel. Plaintiff NuStar's Rule 30(b)(6) designee, Anthony Nunes III admitted having no idea who was paying Plaintiffs' lawyers.

Congressman Nunes is closely related to the individual Plaintiffs and has a history of litigation against media defendants, including a lawsuit in this Court about this same story. *Nunes v. Lizza et al.*, 19-CV-4064. [2]

II. DISCUSSION

A. The Parties' Contentions

If the instant lawsuit is controlled by "wealthy private donors," perhaps related to the Congressman, Defendants contend this raises significant constitutional concerns. First, Defendants generally are concerned about the "chilling effect" of financing defamation cases. Second, more specifically, Defendants raise the specter of private figures pursuing "tandem libel cases" at the behest of a public figure and avoiding the protections offered to media defendants by the requirement of proving actual malice. Defendants also

contend that evidence of third-party funding of Plaintiffs' lawsuit will be relevant to whether Plaintiffs should be considered "involuntary limited purpose public figures," an argument Defendants have previously raised. (Doc. 37 at 38-41.) If they are public figures, Plaintiffs would have to show actual malice – something Defendants claim they cannot show. Defendants argue the information is relevant to Plaintiffs' standing. Defendants contend information about funding of the litigation will show if Plaintiffs' case is a "mere surrogate" for Congressman Nunes's case, which was recently revived by the Eighth Circuit Court of Appeals. Defendants argue they need information about third-party funding to determine whether Plaintiffs are the parties who will benefit from the case, or if the true beneficiary is Congressmen Nunes, who Defendants believe seeks to further an agenda of intimidating media outlets.

***2** Defendants also contend that they are entitled to the discovery to ascertain if Plaintiffs are the real party in interest as required by Federal Rule of Civil Procedure 17(a). Defendants raise similar concerns about disclosures for conflicts purposes under Rule 7.1. Defendants also contend information about third-party litigation funding would rebut Plaintiffs' narrative of a large media corporation prying into the lives of small-town farmers.

Much of Plaintiffs' resistance is taken up with allegations about Defendants' disclosure of materials designated as "Counsel's Eyes Only" discovery materials. Those allegations are more properly taken up by the Court in response to Plaintiffs' Motion for Sanctions. (Doc. 155.) Plaintiffs' resistance points to media coverage of the disclosure and describes Defendants' "obsession" with uncovering the source of funding. (Doc. 153 at 5.) Plaintiffs note my comments during a January 2021 status conference where I questioned the relevance of the source of funding. In contrast, Plaintiffs' resistance is extraordinarily light on legal reasoning that might support Plaintiffs' objection. I presume from Plaintiffs' discussion of relevancy that relevance figures in their objections. But nowhere in their resistance do they expressly assert the funding sources are irrelevant, much less engage with the issue. Plaintiffs do not object that disclosure of their funding sources would interfere with their First Amendment right of association or invade the attorney-client privilege. *See* *Conlon v. Rosa*, Nos. 295907, 295932, 2004 WL 1627337, at *3 (Mass. Land Ct. July 21, 2004) (citing *NAACP v. Alabama*, 357 U.S. 449, 462 (1958)).

To the extent Plaintiffs engage with the issue presented, Plaintiffs simply make bald denials such as, "There has been no 'coordination' between Plaintiffs and Devin Nunes regarding the lawsuit," "Devin Nunes does not have a 'policy to sue media outlets,' " and "The Plaintiffs are private individuals." (Doc. 153 at 8.) They argue that Defendants are merely speculating about the involvement of third-party funding. (*Id.* at 9.) However, while Plaintiffs are adamant in their assertions that they are not coordinating their respective lawsuits with Congressman Nunes, they do not deny the existence of third-party funding.

B. Standards

Rule 26(b)(1) of the Federal Rules of Civil Procedure provides:

> Unless otherwise limited by court order, the scope of discovery is as follows: Parties may obtain discovery regarding any nonprivileged matter that is relevant to any party's claim or defense and proportional to the needs of the case, considering the importance of the issues at stake in the action, the amount in controversy, the parties' relative access to relevant information, the parties' resources, the importance of the discovery in resolving the issues, and whether the burden or expense of the proposed discovery outweighs its likely benefit. Information within this scope of discovery need not be admissible in evidence to be discoverable.

Rule 34(a) provides for discovery by production requests "within the scope of Rule 26(b)." A party may obtain, as of right, discovery "relevant to any party's claim or defense." 8 Charles Alan Wright & Arthur R. Miller, *Federal Practice & Procedure* § 2008 (3d ed. 2010). As this Court has previously stated:

> The Federal Rules of Civil Procedure authorize broad discovery. *See* Fed. R. Civ. P. 26(b)(1) ("Parties may obtain discovery regarding any nonprivileged matter that is relevant to any party's claim or defense."). "Discovery

> Rules are to be broadly and liberally construed in order to fulfill discovery's purposes of providing both parties with 'information essential to the proper litigation of all relevant facts, to eliminate surprise, and to promote settlement.' " *Marook v. State Farm Mut. Auto. Ins. Co.*, 259 F.R.D. 388, 394 (N.D. Iowa 2009) (quoting *Rolscreen Co. v. Pella Prods.*, 145 F.R.D. 92, 94 (S.D. Iowa 1992)).
>
> ***3** The scope of permissible discovery is broader than the scope of admissibility. *See, e.g., Hofer v. Mack Trucks, Inc.*, 981 F.2d 377, 380 (8th Cir. 1992). Discovery requests are typically deemed relevant if there is any possibility that the information sought is relevant to any issue in the case. *Penford Corp. v. National Union Fire Ins. Co.*, 265 F.R.D. 430, 434–35 (N.D. Iowa 2009) (citing *Davis v. Union Pacific R.R. Co.*, No. 4:07CV00521 BSM, 2008 WL 3992761 (E.D. Ark. Aug. 26, 2008)). Nonetheless, there must be at least a "threshold showing of relevance" before parties "are required to open wide the doors of discovery and to produce a variety of information which does not reasonably bear upon the issues in the case." *Hofer*, 981 F.2d at 380. The party resisting production of requested information bears the burden of establishing the lack of relevancy, unless that lack of relevancy is obvious. *Marook*, 259 F.R.D. at 394–95.

Kampfe v. Petsmart, Inc., 304 F.R.D. 554, 557 (N.D. Iowa 2015). Here, as in *Kampfe*, the issue is whether "there is any possibility that the information sought is relevant to any issue in the case." *Id.* (citing *Penford*, 265 F.R.D. at 434–35).

Discovery must also be

> proportional to the needs of the case, considering the importance of the issues at stake in the action, the amount in controversy, the parties' relative access to relevant information, the parties' resources, the importance of the discovery in resolving the issues, and whether the burden or expense of the proposed discovery out-weighs its likely benefit.

Fed. R. Civ. P. 26(b)(1). "The parties and the court have a collective responsibility to consider the proportionality of all discovery and consider it in resolving discovery disputes." Fed. R. Civ. P. 26(b)(1) advisory committee's note to 2015 amendment.

C. Analysis

1. *The discovery sought is proportional to the needs of the case.*

Plaintiffs have not objected that the discovery is disproportional to the needs of the case. Any concern regarding the proportionality of the discovery is easily disposed of. At the hearing, Plaintiffs' counsel represented that Plaintiffs response to the request, if compelled, would consist of approximately four pages. Thus, it seems that the response would be quite readily made without any burden.

2. *The discovery is relevant.*

The relevancy analysis is somewhat more complex. Although Plaintiffs emphasize that the funding of the litigation is irrelevant to their defamation claim, the scope of discovery is not limited to that claim but extends to Defendants' own "claim[s] and defense[s]." Rule 26(b)(1). *Fulton v. Foley* addressed the relevancy of litigation funding in the context of a claim for wrongful arrest and conviction. 17-CV-8696, 2019 WL 6609298, at *1 (N.D. Ill. Dec. 5, 2019). *Fulton* commenced its analysis with an observation consistent with my initial reaction expressed to the parties in a January 21, 2021 status conference: "As a general matter, courts across the country that have addressed the issue have held that litigation funding information is generally irrelevant to proving the claims and defenses in a case." *Id.* at *2. *Fulton* then helpfully compiled a collection of cases that have addressed discovery of litigation funding: *In re Valsartan N-Nitrosodimethylamine (NDMA) Contamination Products Liab. Litig.*, 405 F. Supp. 3d 612 (D.N.J. 2019) (multidistrict litigation regarding contaminated medication); *Benitez v. Lopez*, 17-CV-3827-SJ-SJB, 2019 WL 1578167, at *1 (E.D.N.Y. Mar. 14, 2019) (civil rights lawsuit); *Miller UK Ltd. v. Caterpillar, Inc.*, 17 F. Supp. 3d 711 (N.D. Ill. 2014) (misappropriation of trade secrets); *Kaplan v. S.A.C. Cap. Advisors, L.P.*, 12-CV-9350 (VM) (KNF), 2015 WL 5730101, at *2 (S.D.N.Y. Sept. 10, 2015) (class action); *Space Data Corp. v. Google LLC*, 16-CV-03260 BLF (NC), 2018 WL 3054797, at *1 (N.D. Cal. June 11, 2018) (nature of underlying dispute not disclosed in ruling); *MLC Intell. Prop., LLC v. Micron Tech., Inc.*, 14-CV-03657-SI, 2019 WL 118595, at *1 (N.D. Cal. Jan. 7, 2019) (patent dispute); *Yousefi v. Delta Elec. Motors, Inc.*, C13-1632RSL, 2015 WL

11217257, at *2 (W.D. Wash. May 11, 2015) (nature of underlying dispute not disclosed in ruling).

***4** There is much that is interesting and helpful about the analysis in the cases *Fulton* cites, but none of them is on all fours with the case at bar. Unsurprisingly, none involves a dispute between a prominent U.S. Congressman and a media conglomerate engaged in a highly-publicized and contentious defamation case. Nevertheless, as *Fulton* observed, "discovery issues are generally case-specific and deserve individual consideration that require courts to balance the concerns of relevancy and proportionality." 2019 WL 6609298, at *2. Expanding on *Fulton's* analysis, *V5 Techs. v. Switch, Ltd.* reasoned as follows:

> Nonetheless, there is no bright-line prohibition on such discovery. Discovery into litigation funding is appropriate when there is a sufficient factual showing of "something untoward" occurring in the case; "[f]or example, discovery will be [o]rdered where there is a sufficient showing that a non-party is making ultimate litigation or settlement decisions, the interests of plaintiffs or the class are sacrificed or not being protected, or conflicts of interest exist." Mere speculation by the party seeking this discovery will not suffice. Courts will compel discovery into funding sources only upon the presentation of "some objective evidence" that the discovering party's "theories of relevance are more than just theories."

334 F.R.D., 306, 311–12 (D. Nev. 2019) (internal citations omitted), *aff'd sub nom. V5 Techs., LLC v. Switch, LTD.*, 2:17-CV-2349-KJD-NJK, 2:17-CV-2349-KJD-NJK, 2020 WL 1042515 (D. Nev. Mar. 3, 2020). I conclude that *V5 Techs* provides a useful framework for this analysis.

In the case at bar, I find there is more than speculation or mere theory regarding the relevance of third-party funding. First, Plaintiffs have not denied that the litigation is being funded by others. Second, Plaintiffs have only incurred $500 in charges during this protracted litigation. Third, Anthony Nunes III, an individual Plaintiff and the corporate representative has "no idea" who is paying the lawyers representing Plaintiffs. These circumstances may not ultimately turn out to be "untoward," but they are certainly unusual. Moreover, these circumstances lift the basis for Defendants' inquiry above the level of mere speculation and raise legitimate subjects for inquiry not present in a more run-of-the-mill personal injury case or commercial dispute. The instant case is distinguishable from a case like *Benitez* where the defendant seeking litigation funding information could not point out how it might affect the plaintiff's credibility or be used for impeachment. 2019 WL 1578167, at *1.

As Defendants point out, a crucial and often determinative issue in a defamation case is whether a plaintiff needs to prove actual malice. (Doc. 148 at 5.) This Court has expressed doubt about the viability of a theory of defense based on the Plaintiffs' status as involuntary public figures. (Doc. 50 at 35.) Nevertheless, the unusual facts presented here make Defendants' inquiry into litigation funding a legitimate subject for discovery to enable them to make the argument on a full record.

Similarly, the Plaintiffs' relationship to Congressman Nunes is an important factor in permitting the discovery. Congressman Nunes has engaged in considerable defamation litigation with the assistance of the same attorney employed by Plaintiffs in the instant action. I offer no criticism of any party's use of the courts to vigorously protect their interests. Nevertheless, Congressman Nunes is clearly a public figure who would be required to prove actual malice. The requirement of actual malice was adopted by the United States Supreme Court because "[i]t would give public servants an unjustified preference over the public they serve, if critics of official conduct did not have a fair equivalent of the immunity granted to the officials themselves." *New York Times v. Sullivan*, 376 U.S. 254, 282-83 (1964.) It may turn out that there has been no coordination between the Congressman and his family, as Plaintiffs assert. However, Defendants inquiry into third-party funding serves the legitimate purpose of determining whether such coordination exists. In light of the important constitutional protections that proof of actual malice provides, it is not a significant imposition to require Plaintiffs to provide discovery that would prove or dispel the notion that a third party is using the instant case to avoid a significant hurdle to a defamation claim. Given the close family relationship, the other defamation litigation Congressman Nunes has pursued in his own name with the help of the same attorney, and the Plaintiffs' lack of knowledge of who is paying their lawyers, the inquiry is not founded on mere speculation.

***5** These circumstances also justify discovery of third-party funding based on the other reasons advanced by Defendants. Plaintiffs filed a Financial Interest Disclosure Statement that provides:

> Pursuant to Rule 7.1 of the Federal Rules of Civil Procedure and Local Civil Rule 7.1(a) of the United States District Court for the Northern District of Iowa and to enable Judges and Magistrate Judges to evaluate possible disqualification or recusal, the undersigned counsel for Plaintiff, NuStar Farms, LLC ("NuStar"), in the above captioned action, certifies that there are no associations, firms, partnerships, corporations, and other artificial entities that either are related to NuStar as a parent, subsidiary, or otherwise, or have a direct or indirect pecuniary interest in the Plaintiffs' outcome in the case. There are no parents, trusts, subsidiaries and/or affiliates of NuStar that have issued shares or debt securities to the public.

(Doc. 3 at 1.) I will not engage in speculation about what arrangements Plaintiffs may have made to finance their lawsuit, if any. However, Anthony Nunes III professed lack of knowledge about who is paying Plaintiffs' lawyers at least raises the possibility that an undisclosed entity related to NuStar has a pecuniary interest in the outcome of the case that would be pertinent to the Court's assessment of conflicts.

Additionally, an action must be prosecuted in the name of the "real party in interest." Fed. R. Civ. P. 17(a)(1). *Suda v. Weiler Corp.*, noted:

> Rule 17(a) was designed to serve dual purposes. First, it serves "to protect the defendant against a subsequent action by the party actually entitled to relief, and to ensure that the judgment will have a proper res judicata effect." *Intown Properties Mgmt., Inc. v. Wheaton Van Lines*, Inc., 271 F.3d 164, 170 (4th Cir. 2001) (citation omitted). Second, it is designed to avoid the unjust forfeiture of claims. *See Sun Refining & Mktg. Co. v. Goldstein Oil Co.*, 801 F.2d 343, 345 (8th Cir. 1986). "Although the district court retains some discretion to dismiss an action where there was no semblance of any reasonable basis for the naming of an incorrect party, there plainly should be no dismissal where substitution of the real party in interest is necessary to avoid injustice." *Advanced Magnetics, Inc. v. Bayfront Partners, Inc.*, 106 F.3d 11, 20 (2d Cir. 1997) (quotation and citations omitted).

250 F.R.D. 437, 440 (D.N.D. 2008). I cannot say, based on the record before me, that NuStar is not a real party in interest. However, I also cannot rule out the possibility. Anthony Nunes III's lack of knowledge about who is paying the attorneys prosecuting this action raises legitimate concern about not only who may be in charge of the lawsuit, but also whether Plaintiffs are the still the real parties in interest. Defendants call the Court's attention to *Conlon v. Rosa*, which raised the concern of secret funding by stating, "He who pays the piper may not always call the tune, but he'll likely have an influence on the playlist." 2004 WL 1627337, at *2.

Again, I will refrain from speculating about the terms of any agreement between Plaintiffs and a third-party who may be funding this litigation. Nevertheless, it is more than mere speculation and far from a "fishing expedition" to make inquiries that would determine if Plaintiffs assigned all or some of their interest in their claims. Plaintiffs claim compensatory damages of $20,000,000. (Doc. 51 at 1.) It is not unreasonable to inquire whether Plaintiffs' arrangement with whomever may be funding the case includes an assignment or an agreement that the funder otherwise stands to benefit from the litigation's outcome. If Plaintiffs have made such an assignment, they may no longer be the real parties in interest. Defendants have a legitimate interest in ensuring the judgment will have a preclusive effect. *See e.g.*, *TCF Nat. Bank v. Mkt. Intel., Inc.*, Civil No. 11-2717 (JRT/AJB), 2012 WL 3031220, at *10 (D. Minn. July 25, 2012) (allowing discovery to proceed to identify real parties in interest).

***6** Similarly, Defendants raise a concern that "one of the witnesses" in this case may be involved in funding the litigation. (Doc. 148 at 9.) "Courts have found that indemnification agreements between co-defendants, including agreements regarding the payment of defense fees and costs, are relevant to credibility issues and a proper subject of discovery." *Kaplan*, 2015 WL 5730101, at *2. I gather from comments at the hearing that Defendants' concern is that Congressman Nunes may be a source of, or helped arrange, the funding. While this concern has yet to be proven, the basis for it goes beyond mere conjecture. Congressman Nunes and Mr. Biss have related litigation in this Court arising from the same allegedly defamatory article at issue here. Congressman Nunes alleges significant damages arising from the article, as do Plaintiffs. While these

family members may be separately financing their respective suits, it is not merely a fishing expedition to inquire about the Congressman's involvement in the financing of the instant lawsuit and his stake, if any, in the outcome. It may be that he has no more than a desire for his family to succeed in their lawsuit. However, he is also a witness in this case and Defendants are entitled to inquire about his interests in the lawsuit that may illuminate a possible bias.

Finally, the records are relevant to respond to a "David vs. Goliath" narrative. Certainly, Plaintiffs' Second Amended Complaint previews this narrative[3] and no one who has spent any time trying cases would be surprised by such a theme. *Contl. Cirs. LLC v. Intel Corp.* addressed discovery of litigation funding to permit a defense response to the narrative:

> [The discovery requests] concern Plaintiff's financial resources and could be used to refute any David vs. Goliath narrative at trial. Plaintiff claims that any such narrative is speculative, but Defendants are entitled to conduct discovery that may refute potential trial themes, and Defendants note that at least some evidence suggests that such a narrative will be asserted in this case.

435 F. Supp. 3d 1014, 1019 (D. Ariz. 2020).

For the foregoing reasons, I overrule Plaintiffs' relevance objection.

D. Documents will be subject to in camera inspection.

Defendants suggest I make an *in camera* inspection of the records Plaintiffs produce in response to Request No. 92 to assure the items produced are properly discoverable and relevant. (Doc. 148 at 10.) Plaintiffs resist the production, but make no reference to the need for an *in camera* inspection in their resistance. (Doc. 153.) I conclude it is prudent to review the records prior to requiring production to Defendants. If, after my *in camera* review, no reason appears to reconsider my decision, I anticipate entering a supplemental order requiring their production to Defendants consistent with the protective order in place.

III. CONCLUSION

Defendants' Motion to Compel Responses to Third-Party Litigation Funding Discovery Requests (Doc. 147) is **granted**. Plaintiffs shall deliver to my chambers by email and/or hard copy by November 2, 2021 all records in their possession responsive to Request No. 92 for an *in camera* inspection.

IT IS SO ORDERED this 26th day of October, 2021.

All Citations

Not Reported in Fed. Supp., 2021 WL 7186264

Footnotes

1 Defendants failed to attach to their motion a copy of the disputed request and response as required by LR 37(b). However, because they quoted the single disputed request and the response in their entirety, the omission is harmless. Defendants are adjured to comply with the local rules.

2 Congressman Nunes's lawsuit was dismissed by this Court but revived by the Eighth Circuit Court of Appeals. As of the date of this order, mandate has not issued and a petition for *en banc* review remains pending.

3 For example, Plaintiffs assert: "Plaintiffs are private individuals. They operate a private business and live with family in the small community of Sibley, Iowa. They are active in the local community in Sibley, and have

always been involved in giving and fundraising for their local church." (Doc. 51 at 2 ¶ 1.) Plaintiffs describe Defendant Hearst as follows:

> Hearst's headquarters and principal place of business is in New York. Hearst publishes *Esquire* magazine. Hearst is a unit of Hearst Corporation, a global media, information and services company. Hearst's print and digital assets reach 155 million readers and site visitors each month – two-thirds of all millennials, and over 80% of Gen Z and millennial women in the country."

(*Id.* at 4 ¶ 7.)

THE ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK
COMMITTEE ON PROFESSIONAL ETHICS

FORMAL OPINION 2024-2: ETHICAL ISSUES ARISING FROM ADVICE TO CLIENTS ON CLIENT-FUNDER LITIGATION FUNDING AGREEMENTS

TOPIC: **LITIGATION FUNDING**

DIGEST: Clients who would like to obtain, or who have obtained, litigation funding (usually referred to as "client-directed litigation funding") sometimes ask a lawyer representing them in the litigation that is to be the subject of the funding to review the litigation funding agreements on the client's behalf. Many times, a funder will ask the lawyer to become a party generally to the funding agreement, acknowledge it, or acknowledge and agree only to portions. Lawyers must consider not only the relevant substantive law, but their ethical obligations when advising on, agreeing to, or acknowledging an agreement. This opinion addresses some of the most common ethical issues and offers guidance. This opinion is divided into four sections: (1) an introduction to litigation funding, (2) pre-contractual issues, (3) contractual issues, and (4) post-contractual issues.

RULES: **1.0, 1.1, 1.2, 1.4, 1.6, 1.7, 1.8, 1.9, 1.15, 1.16, 5.4, and 5.7**

QUESTION: What are a lawyer's ethical duties when advising a client about litigation funding agreements the client intends to enter with a funder?

OPINION:

Introduction

Litigation funding is when a third party – someone with no legal or equitable interest in a claim – provides money or anything of value in exchange for a promise for some payment if the claim is settled or resolved in the claimholder's favor.[1] "Lawyer-directed funding" refers to a situation where the third party contracts directly with a lawyer. "Client-directed funding" which is the subject of this opinion, refers to a situation where there is a contract between a third party and a claimholder in which the parties agree that funds provided by the third party will be used by the claimholder to pay for a lawyer's fees and litigation expenses in exchange for a promise by the claimholder to pay the third party a sum of money sourced from the proceeds of the claim if and

* *Originally issued in April 2024; revised June 2024*

[1] Litigation funding is considered to be "champerty" in some parts of the United States, but litigation funding, as that term is used in this Opinion, is not champerty in New York. New York Judiciary Law (which defines the misdemeanor of champerty) prohibits the assignment of certain choses-in-action. N.Y. Judiciary Law §§ 488 & 489. In the typical litigation funding transaction in New York, no chose-in-action is assigned. Litigation funding contracts may employ the language of assignment (although they need not), but even when they do, usually all that is assigned are the proceeds from a chose-in-action.

only if the claim generates proceeds.[2] The last major review of client-directed funding by this Bar Association, which this opinion updates, was in 2011.[3]

Litigation funding is a rapidly growing area of financial activity. It has the potential to increase access to justice by creating new opportunities for access to capital for claimants and their lawyers. But lawyers with clients who seek litigation funding may be confronted by novel issues of law and professional responsibility.

I. Pre-Contractual Issues

A. Sharing of Fees with Non-Lawyers

Rule 5.4(a) prohibits lawyers from "shar[ing] legal fees with a nonlawyer." It is intended to prohibit "*any* financial arrangement in which a nonlawyer's profit or loss is directly related to the success of a lawyer's legal business."[4] It has various rationales, but it is clear that it is intended to serve two overarching purposes – to protect clients from non-lawyers' interference with their lawyers' independence of professional judgment and to prevent the unauthorized practice of law by non-lawyers. New York City Opinion 2018-5 stated that "Rule 5.4(a) forbids a funding arrangement in which the lawyer's future payments to the funder are contingent on the lawyer's receipt of legal fees or on the amount of legal fees received in one or more specific matters." The Committee explicitly noted that client-directed funding – where the payments to the funder flow from the client's recovery and not the lawyer's fee – does not implicate Rule 5.4(a) and thus does not violate the Rules of Professional Conduct because such funding does not involve a sharing of fees.[5]

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[2] There is also a variation of "client-directed funding" in which the parties agree that funds provided by the third party will be used by the claimholder to pay for lawyers' fees and litigation expenses and where the third party requires the claimholder to repay the third party up to the original sum advanced if the claim generates proceeds. This is typical of client-directed funding by non-profit organizations.

[3] N.Y. City Op. 2011-2. This Committee considered lawyer-directed funding in N.Y. City Op. 2018-5.

[4] HAZARD, ET. AL., THE LAW OF LAWYERING (4TH ED.), at 155.

[5] N.Y. City Op. 2018-5. This is true even if the lawyer is a signatory to the agreement between the client and the funder. Shortly after the publication of Opinion 2018-5, the New York City Bar Association formed a working group, tasked with evaluating "whether Rule 5.4, as interpreted in Opinion 2018-5, well serves the professional community and the public, or whether the Rule should be revised to reflect contemporary commercial and professional needs and realities." REPORT TO THE PRESIDENT BY THE NEW YORK CITY BAR ASSOCIATION WORKING GROUP ON LITIGATION FUNDING (February 28, 2020), at 23, http://documents.nycbar.org/files/Report_to_the_President_by_Litigation_Funding_Working_Group.pdf (All websites last accessed on March 26, 2024). The working group proposed two versions of revisions to Rule 5.4, both providing that lawyers could engage in lawyer-directed legal finance, albeit under different conditions. The New York City Bar Association Professional Responsibility Committee issued a report on April 5, 2024 on lawyer-directed funding and Rule 5.4 incorporating various aspects of the Working Group proposals but differing from both of them. The proposal would allow a lawyer or law firm to pay, assign, pledge or give a security interest in earned or unearned legal fees to a nonlawyer for representing one or more specific clients provided that the lawyer provides the client(s) with (1) written notification and (2) an opportunity to inquire. *See* NYCBA Committee on Professional Responsibility, *Proposed Amendments to New York Rule of Professional Conduct 5.4 as Concerns Non-Party Litigation Funding*, (April 2024) https://www.nycbar.org/reports/proposed-amendments-to-ny-rule-of-professional-conduct-non-party-litigation-funding/?back=1.

B. Scope of Representation

Lawyers may advise clients about litigation funding. If a client has decided to secure funding but does not have a particular funding company in mind, a lawyer may refer the client to one or more companies.[6] New York City Opinion 2011-2 opines that, for a lawyer to make a referral, the lawyer "should conduct a reasonable investigation to determine whether particular providers are able and willing to offer financing on reasonable terms." If the lawyer wishes to provide the recommendation as a nonlegal service, Rule 5.7(a)(4) requires the lawyers to advise the client in writing that "the services are not legal services and that the protection of a client-lawyer relationship does not exist with respect to the nonlegal services," or the client may presume that the services are to be the subject of the lawyer-client relationship. Thus, unless the lawyer satisfies the requirements of Rule 5.7(a)(4), the Rules of Professional Conduct, including the duty of competence, will apply to the making of the referral.

Lawyers may also represent existing clients in transactions with litigation finance companies and may charge clients a fee for such representations in addition to the fee agreed to for the underlying representations.[7] Litigation funding agreements often include complicated waterfall financing provisions and securitization terms. The litigation funding contract may involve terms of art and there may be questions about the clients' underlying legal matter and the potential obligations of the client to the funder based on the covenants in the contract, including whether the contract is enforceable. As with any advice that lawyers are asked to provide, a lawyer who offers advice to clients about litigation funding, or who communicates with litigation funding companies on behalf of a client concerning litigation funding agreements already in existence, must do so competently and advise the client if the lawyer is unable to do so.[8]

C. Conflicts of Interest

When clients seek advice about potential funding, lawyers must think carefully about the potential conflicts involved in providing this advice.

First, may a lawyer represent both a funder and a litigant (whom the lawyer is representing) in evaluating a pending or potential lawsuit? Such a joint representation arrangement, while atypical, would serve to provide privilege protections for the lawyer's advice to the joint clients. While both the funder and the litigant have aligned interests in understanding the strengths and weaknesses of the matter, they may also have differing interests. Comment 8 to Rule 1.7 states that differing interests exist where there is "a significant risk that a lawyer's exercise of professional judgment in considering, recommending or carrying out an appropriate course of action for the client will be adversely affected." If the client's goal is to obtain funding even for a weak claim, and the funder's goal is to fund only strong claims, these interests may conflict. Notwithstanding differing interests, such a joint representation may be consentable under Rule 1.7(b), depending on its specific facts, and the consent would need to include an agreement by both the litigant and the funder that there are no confidences or privileges as between joint clients

[6] N.Y. State Op. 666 (1994).

[7] N.Y. State Op. 769 (2003).

[8] Rule 1.1.

with respect to the joint representation. However, if a lawyer wants to subsequently represent the funder or the litigant in connection with the negotiation of the funding agreement after a limited joint representation to provide an evaluation, that would likely require a conflict waiver under Rule 1.9(a). This is because the other former client would be materially adverse in what is likely a substantially related matter; *i.e.*, the terms of the funding agreement will likely be informed by the evaluation that the lawyer jointly performed for the funder and the litigant.

If a lawyer determines that a joint representation is not possible, or if either party refuses to consent, then the lawyer should only provide an evaluation of the claim(s) to the party or parties that retain the lawyer. Further, as discussed below, the lawyer should caution the client about the risks to privilege of sharing any such evaluation with a funder.[9] The decision of whether to share is the client's.[10]

Where lawyers are engaged directly by a funder to evaluate a claim or negotiate a contract, they may want to seek an advance conflict waiver to ensure that the litigation funder does not seek to disqualify them in unrelated lawsuits. Recurrently handling a certain type of matter for a former client does not preclude a lawyer from later representing another client in a factually distinct problem of that type under Rule 1.9.[11] But a litigation funder may argue that the lawyers obtained the funder's confidential information, including funding or contracting strategy, that could in certain circumstances be used in unrelated litigation to the funder's disadvantage when the lawyers advise clients on, for instance, how to seek contractual concessions from the funder.[12]

Lawyers also must consider potential personal interests that put the lawyers in conflict with the client when the client asks for legal advice about funding a litigation the lawyer has filed or been retained to file. Where a lawyer knows that funding is necessary for the client to proceed with the action or continue to pursue a matter handled by the lawyer, Rule 1.7 does not require the lawyer to advise the client of the existence of a personal conflict of interest. The lawyer's interests in the client's funding, while material to the lawyer's own personal interest, are no different than a case where lawyers know that the client will only retain them on an hourly basis to pursue a claim if they opine that the claim is likely to succeed.

On the other hand, after the initial funding contract has been executed, a lawyer may be faced with additional potential conflicts of interest if the funder and client decide to renegotiate or extend the funding agreement and the lawyer's receipt of payment for completed work depends on the continuation of the funding. At that point, the funder may wish to add new terms which, had they been proffered at the outset of the funding relationship, the lawyer may have felt free to advise the client to reject, but which, now that the lawyer is in the midst of the representation, the lawyer may be less willing to advise the client to reject. In this case, unless the client expressly waives

[9] N.Y. City Op. 2018-5.

[10] Rule 1.2(a).

[11] Rule 1.9, comment 2.

[12] Rule 1.9(b)(2); Rule 1.7(a)(1).

this additional conflict in writing after full disclosure by the lawyer, the lawyer should recommend to the client that separate counsel be retained to negotiate the revision of the funding agreement.[13]

A personal interest conflict under Rule 1.7 may arise because of lawyers' investment in, receipt of a referral fee from, or relationship with a litigation funder.[14] Neither lawyers nor their firms may represent clients in litigation funded by a litigation funder in which one of the firm's lawyers is an investor.[15] Nor may lawyers refer clients to a funder in which that lawyer or another lawyer in their firm owns an interest.[16] This prohibition is nonwaivable because it is much like the situation where lawyers may not refer a client to a title abstract company in which they own an interest.[17] In the context of a title insurance company owned by a lawyer, a lawyer may ask a client to waive a personal financial conflict of interest in connection to a nonlegal service only where a disinterested lawyer would "believe that the representation of the client will not be adversely affected."[18] Like title insurance, the economic interests of a funder and a client are sufficiently in conflict that the lawyer's representation of the client would be adversely affected. Furthermore, Rule 1.8(i) states that "[a] lawyer shall not acquire a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client" except through a lien or reasonable contingent fee. The comments to this rule explain that it has its basis in the common law doctrines of champerty and maintenance, and that it is intended to "avoid giving the lawyer too great an interest in the representation."[19]

D. Special Considerations When the Funder is a Not-For-Profit.

There are no separate rules for funders that are not-for-profit.[20] However, special considerations must be taken into account when a firm represents a client on a pro bono basis and a not-for-profit funder related to the firm provides funds to the client to pay for litigation-related expenses.

There, even if the firm has a financial interest in or controls the not-for-profit funder (directly or indirectly), the not-for-profit may provide the client with funds so long as the purpose of the financing is not to make a profit and the funding is limited to payments to cover expenses of

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[13] Although outside the scope of this opinion, the Committee observes that the lawyer may want to propose to the client that, in this circumstance, it may be equitable for the funder to pay for the cost of the client's separate counsel.

[14] "[T]he lawyer is barred from accepting a referral fee from the company if the fee would impair the lawyer's exercise of professional judgment in determining whether a financing transaction is in the client's best interest and would compromise the lawyer's ethical obligation to provide candid advice regarding the arrangement; even where the fee is permitted, the lawyer may be required to remit the fee to the client." N.Y. City Op. 2011-2.

[15] N.Y. State Op. 1145 (2018).

[16] N.Y. State Op. 666 (1994); N.Y. State Op. 769 (2003).

[17] N.Y. State Op. 595 (1988).

[18] N.Y. State Op. 731 (2000).

[19] Rule 1.8, comment 16.

[20] Not-for-profit litigation funding has been recognized by the U.S. Supreme Court as protected by the First Amendment against certain exercises of the state's police powers. *See NAACP v. Button*, 371 U.S. 415, 442 (1963) (holding that not-for-profit's support of civil rights litigation was a "constitutionally privileged means of expression to secure constitutionally guaranteed" rights).

the litigation. In New York State Opinion 1145 (2018), the committee found that neither a lawyer nor the lawyer's firm may represent a client in litigation funded by a litigation financing company in which the lawyer is an investor. The opinion was driven by concerns with conflict-of-interest rules related to the lawyer's financial interest, and those concerns are not implicated where there is no profit motive. In addition, Rule 1.8(e)(1) allows a lawyer to advance "court costs" or litigation expenses for a client's litigation, repayment of which is contingent on the outcome of the matter. Therefore, because a lawyer may do indirectly what they may do directly, it follows that New York State Opinion 1145 does not prohibit a firm from representing a client in a matter where the court costs and litigation expenses are advanced by a not-for-profit funder related to the law firm providing the pro bono representation.

This does not mean, however, that a law firm providing pro bono services may represent a client in a matter where the firm's fees (hourly or otherwise determined) are advanced by a not-for-profit funder related to the firm. A lawyer may not provide "financial assistance" to a client except under the limited exceptions set out in Rules 1.5 and 1.8, and because paying a firm's fees on behalf of a client are not within those exceptions, the fees cannot be advanced to the client by a not-for-profit funder that is related to the firm.

II. Contractual Issues

A. Consistency with New York and other law

Rule 1.2(d) states that a lawyer "shall not counsel a client to engage, or assist a client, in conduct that the lawyer knows is illegal or fraudulent, except that the lawyer may discuss the legal consequences of any proposed course of conduct with a client." While litigation finance contracts are generally enforceable in New York, the same litigation finance contract may not be enforceable under the law of another jurisdiction.[21] A lawyer may assist a client by preparing a contract that employs terms that may prove to be voidable (so long as the lawyer does not "know"[22] that the client intends to accept the benefits of the contract but then use the voidability to avoid any burdens), but then the lawyer must advise the client of the risks connected to adopting those contract terms.[23] Assuming the client is provided adequate information to make such a decision, the client may instruct the lawyer to employ those terms.[24]

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[21] For example, a litigation funding agreement that would have been enforceable under New York law would not have been enforceable under Minnesota law until 2020. A litigation funding agreement that would have been enforceable had it been performed in New York would not have been enforceable had it been performed in Minnesota, even if it contained New York choice of law and choice of forum selection clauses. *See Maslowski v. Prospect Funding Partners LLC*, 890 N.W.2d 756, 767 - 68 (Minn. Ct. App. 2017) (holding that facts of transaction require contract law of Minnesota, not New York, apply); and *Prospect Funding Holdings L.L.C v. Maslowski*, 146 A.D.3d 535, 535 (1st Dep't 2017) (deferring to Minnesota courts on question of choice of law in this matter).

[22] *See* Rule 1.0(k) for the definition of "know."

[23] *See* N.Y. State Op. 584 (1987) ("If the lawyer is satisfied that the contract or activity is not illegal but instead determines that it is, at worst, voidable or unenforceable, there is nothing in Canon 7 or elsewhere in the Code of Professional Responsibility to prohibit the lawyer from drafting such a contract or assisting in such conduct, provided the risks inherent therein (that the contract may be voidable or unenforceable or the conduct may otherwise be challenged) are discussed with the client.").

[24] Rules 1.2(a) and 1.4(b).

B. Funder Payment and Withdrawal

Lawyers sometimes structure their funded engagements to allow clients to fulfill their payment obligations by using their own funds or third-party funds.

If the engagement is structured such that the only payment obligation is on the litigation funder, lawyers should be conscious of how this might affect their ability to withdraw upon non-payment. Rule 1.16(c)(5) provides that a lawyer may withdraw from a representation when "the client deliberately disregards an agreement or obligation to the lawyer as to expenses or fees." Therefore, if there is no obligation on the client to make payment to a lawyer, and the funder fails or refuses to make a payment, then the lawyer cannot rely on this provision of the Rules as the basis to withdraw. However, an engagement letter may specify that lawyers are permitted to withdraw should the funder fail to make payment (or decide to stop funding the litigation) so long as other requirements for withdrawal, such as ensuring that the withdrawal does not have a material adverse effect on the interests of the client and receiving permission from a tribunal where required, are followed.[25]

C. Confidentiality and privilege issues (Rule 1.6)

To evaluate a potential investment and then to monitor an investment after it is made, litigation funders typically seek information and analysis about claims and defenses from clients and the clients' lawyers. Litigation funding agreements often seek to specify the documents that clients and/or lawyers will provide, which may include requests for (a) legal evaluations of claims and defenses prior to or during litigation, (b) copies of material evidence, (c) drafts of filings, and (d) updates by the lawyers (written or oral).

Rule 1.6(a) provides that a lawyer shall not reveal a client's confidential information unless the client gives informed consent, the disclosure is "impliedly authorized to advance the best interests of the client and is either reasonable under the circumstances or customary in the professional community," or for specified preventative and/or defensive purposes not implicated by this opinion.

A lawyer may not disclose client confidential information to a funder without client consent. Although obtaining funding may be "impliedly authorized to advance the best interests of the client," a lawyer should consider whether privilege likely will be waived by disclosure to the funder and whether attorney work product can be protected by the use of a non-disclosure agreement. And although litigation funding has become increasingly common, it is not "reasonable under the circumstances or customary in the professional community" to provide a funder with a client's confidences without the client's express consent.

Although a client may consent or ask for its information to be provided to a funder to secure funding, lawyers must ensure that the client's consent is "informed," as defined by Rule 1.0(j). That rule states that consent is only informed if it comes "after the lawyer has communicated information adequate for the person to make an informed decision, and after the lawyer has

[25] Rule 1.16(c)(10) and (d).

explained the material risks of the proposed course of conduct and reasonably available alternatives."

Here, the most important risk to discuss with the client is that sharing these materials with the funder may waive attorney-client privilege or work product protections. While the substantive laws of privilege and work product are beyond the scope of this opinion, there are cases on both sides of the issue.[26] The most cautious course of action is to disclose only non-protected and/or public materials. Where the funder requires more as a condition of funding, lawyers should seek to guide the client to minimize the risks to privilege to the greatest extent possible.

Whenever lawyers provide confidential information to funders, there should be a non-disclosure agreement with the funders through a standalone non-disclosure agreement during the diligence process or a non-disclosure provision in the litigation funding agreement, or both.

D. Control of litigation

The Rules of Professional Conduct protect both the client's ability to control litigation and lawyers' independent judgment. Funders sometimes seek to reserve for themselves, in the funding contract, rights and privileges related to the client's exercise of authority under Rule 1.2. The funder may require the client to inform it when a settlement offer has been made. The funder also may require the client to inform it if the client wishes to discharge its current lawyer. The funder may impose various remedies on the breach of these covenants, ranging from conversion of the agreement to a recourse loan at a defined interest rate, immediate rescission of the contract, or requiring the client to subject its decision to a review of an arbitrator. Lawyers have a responsibility to advise the client about the implications of such provisions.

Lawyers must abide by clients' decisions concerning the objectives of the matter; must abide by the clients' settlement decisions; and must consult with clients as to how the objectives of the matter are to be pursued.[27] Further, as Comment 2 to Rule 1.2 says, lawyers "usually" defer to clients regarding questions of expenses. Rule 5.4(c) prohibits lawyers from allowing a third party who "recommends, employs or pays" the lawyer to "direct or regulate" the lawyer's professional judgment.[28] There is no conflict between Rule 1.2(a) and Rule 5.4(c). Clients may, by contract, agree to instruct their lawyers in accordance with the wishes of the contract's counterparty, but that does not change the lawyers' obligations to the clients. Lawyers should not "confuse[] freedom of judgment with freedom of action. Lawyers must always have the former,

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[26] *Contrast Miller UK Ltd. v. Caterpillar, Inc.* 17 F. Supp. 3d 711 (N.D. Ill. 2014) (holding that attorney-client privileged materials lost their protection when shared with litigation funders because a "shared rooting interest in the 'successful outcome of a case' . . . is not a common *legal* interest" (emphasis in original)) *with Elm 3DS Innovations LLC v Samsung Elecs. Co.*, 2020 US Dist LEXIS 216796, at *2 (D. Del. Nov. 19, 2020, No. 14-1430-LPS) (holding that documents shared with funders were prepared in anticipation of litigation, and thus protected by the work product doctrine).

[27] Rule 1.2(a).

[28] Rule 5.4(c) cannot be waived by the client under any circumstance (informed consent is no cure), and so no lawyer may participate in the making of a legal funding agreement that requires the client to instruct the lawyer to allow the funder to interfere with the lawyer's independent professional judgment. *See, e.g.*, Mich. Op. RI-321 (2000) (finding that a financing agreement that placed restrictions on an attorney's ability to manage the litigation created an "impermissible conflict of interest" and interfered with the attorney's exercise of professional judgment).

but they rarely, if ever, have the latter, and no rule requires clients to give it to them."[29] This comment was made in response to concerns that lawyers would violate the duty of professional independence if they represented clients who give liability insurers the right to control how lawyers conducted the defense of the client. Rule 1.2's obligations upon lawyers are not affected by the terms of the contract the client has with a third party.[30] In other words, if a client in a litigation funding agreement agrees to accept the funder's instructions to the client about whether to accept or reject a settlement, the lawyer's ethical obligation is unchanged; Rule 1.2 requires the lawyer to follow the client's instructions about whether to settle, regardless of whether the client would be breaching the contract in doing so.[31] Thus, lawyers may not sign funding agreements requiring the lawyers to follow the instructions of the funders rather than lawyers' clients.

Finally, there are limits on lawyers' ability to make contracts with clients that limit the right to discharge the lawyers. "The unqualified right to terminate the attorney-client relationship at any time has been assiduously protected by the courts."[32] This is a principle of contract law drawn from New York public policy reflected in the law governing lawyers, including in the New York Rules of Professional Conduct. No lawyer may violate this principle directly or indirectly. Therefore, no lawyer may agree to a contract in which the client may not freely discharge the lawyer.[33] Nor may lawyers agree with a client not to withdraw from the representation under Rule 1.16(b).[34] By extension, no funder may cause a client to insist on such a promise from lawyers.

III. Post-Contractual Issues

If lawyers are aware of the assignment to the litigation funder of a portion of proceeds from a litigation, they have an obligation to notify the funder when they come into possession of the proceeds and to pay the proceeds out according to the assignment.[35] Rule 1.15(c)(4) requires that lawyers promptly pay to the "client or third person as requested by the client or third person the funds, securities, or other properties in the possession of the lawyer that the client or third person is entitled to receive." The comment to the rule notes that "[a] lawyer may have a duty under applicable law to protect such third party claims against wrongful interference by the client" and specifies that "when the third-party claim is not frivolous under applicable law," as, for example, where there is a contractual assignment of which the lawyer is aware, "the lawyer must refuse to surrender the property to the client until the claims are resolved."[36] Lawyers should not decide the dispute themselves, but may represent their clients in resolving the dispute with the funder. If the

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[29] Charles Silver, *Flat Fees and Staff Attorneys: Unnecessary Casualties in the Continuing Battle over the Law Governing Insurance Defense Lawyers*, 4 CONN. INS. L.J. 205, 230 – 3 (1997) (footnotes omitted).

[30] *See* N.Y. State Op. 1154 (2018) at ¶ 11.

[31] Of course, when representing more than one client, lawyers can work with the clients to designate someone to make decisions on behalf of the client group. Likewise, clients may appoint agents.

[32] *Matter of Cooperman*, 83 N.Y.2d 465, 473 (1994) (citations omitted).

[33] The Committee does not address in this opinion whether lawyers may waive the right to permissive withdrawal.

[34] We do not address whether a lawyer may agree not to exercise the lawyer's right to withdraw under Rule 1.16(c).

[35] *Leon v. Martinez*, 84 N.Y.2d 83, 90 (1994).

[36] Rule 1.15, comment 4.

dispute cannot be resolved through negotiation, lawyers should file an action to have the dispute resolved by a court (or arbitrator if the funding agreement contains an arbitration provision).[37]

Lawyers may, but are not obligated to, agree to represent a client in negotiating a reduction of the payment owed by the client to a legal finance company upon the resolution of litigation if it is not within the scope of the original engagement letter.[38] Lawyers who assume the responsibility for negotiating with a funder on behalf of their clients at the end of the representation must do so competently.

CONCLUSION

Litigation funding is a developing area of law with complex ethical issues, and lawyers who advise clients on client-directed litigation funding should tread carefully.

[37] *Id.*

[38] *See Francis v. Mirman, Markovits & Landau PC*, N.Y. Sup. Ct. Kings County, No. 29993/10, Jan. 3, 2013. It is common for clients in the "consumer" sector of litigation finance to pay less to the funder than required under the contract. *See* Ronen Avraham & Anthony Sebok, *An Empirical Investigation of Third-Party Consumer Litigant Funding*, 104 CORNELL L. REV. 1133, 1157 - 58 (2019). Presumably these reductions are secured through the effort of a client's lawyer. The fact that such conduct may be common does not make it a necessary part of the representation unless the lawyer explicitly offers to provide this service.

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United States District Court, W.D. Wisconsin.

TEAM SCHIERL COMPANIES and Heatland Farms, Inc., Plaintiffs,

v.

ASPIRUS, INC. and Aspirus Network, Inc., Defendants.

22-cv-580-jdp

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Signed December 11, 2024

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OPINION and ORDER

ANITA MARIE BOOR, Magistrate Judge

***1** This proposed class action concerns alleged antitrust violations in the healthcare industry. Before the court is defendants' motion to compel plaintiffs' responses to defendants' interrogatories and requests for admission. Dkt. 116. The disputed information falls into three categories defendants contend are important to class certification and the merits of plaintiffs' claims. Dkt. 117 at 11. For the reasons below, the motion is GRANTED in part and DENIED in part.

BACKGROUND

Plaintiffs Team Schierl Companies and Heartland Farms, Inc. are self-insured employers that purchase healthcare services from defendants Aspirus, Inc. and Aspirus Network, Inc. Dkt. 1 at 14. Plaintiffs allege that defendants have obtained a large share of the healthcare market in north-central Wisconsin through multiple kinds of anticompetitive conduct in violation of Sections 1 and 2 of the Sherman Act. *Id.* at 1. Plaintiffs also assert class action allegations. Dkt. 1 at 41.

Discovery has been open for over 18 months, Dkt. 35, and the court has already weighed in on some discovery issues, Dkt. 115 & Dkt. 140. The parties' most recent dispute concerns: (1) information about a funding agreement for one of plaintiffs' firms; [1] (2) information about the factual basis for plaintiffs' allegations and theories of anticompetitive conduct; [2] (3) and information clarifying the alleged geographic and product market scope. [3] Dkt. 117 at 10–11.

LEGAL STANDARDS

"Parties may obtain discovery regarding any nonprivileged matter that is relevant to any party's claim or defense and proportional to the needs of the case considering the importance of the issues at stake in the action, the amount in controversy, the parties' relative access to relevant information, the parties' resources, the importance of the discovery in resolving the issues, and whether the burden or expense of the proposed discovery outweighs its likely benefit. Information within this scope of discovery need not be admissible in evidence to be discoverable." Fed. R. Civ. P. 26(b)(1). In the class-certification context, information is relevant if it provides answers to the questions common to plaintiffs' claims or if it bears on the other Rule 23(b)(3) requirements. *Drake v. Aerotek, Inc.*, No. 14-cv-216-bbc, 2014 WL 7408715, at *3 (W.D. Wis. Dec. 30, 2014).

ANALYSIS

The court addresses the three categories of discovery identified in defendants' motion in turn.

A. The Funding Agreement

Defendants seek information about the funding one of plaintiffs' law firms receives from Arnold Ventures (Ventures), an LLC founded by Texas billionaire John Arnold, and any other funders not listed in the litigation funding agreement and privilege log that have been produced. Dkt. 117 at 13. Defendants argue that Ventures' outspoken goal of reforming health care through class action litigation may conflict with the goals of potential class members. *Id.* at 14. Defendants reason that the funders may steer the litigation strategy towards sought-after policy outcomes instead of the best interests of the proposed class. *Id.* at 15.

***2** Plaintiffs counter that they have already produced the full agreement between the one law firm and Ventures, and that the agreement states that Ventures cannot exercise any control over this litigation. Dkt. 136-1 at 10. Thus, plaintiffs argue, additional information is irrelevant, citing *In re Hair Relaxer Marketing Sales Practices and Product Liability Litigation*, No. 23-cv-0818, 2024 WL 2133171 (N.D. Ill. April 9, 2024) and other cases. Dkt. 134 at 10.

Plaintiffs have the better argument. Rule 26 permits the discovery of any nonprivileged material that is relevant to any claim or defense. Here, the relevant funding agreement has been produced, and it states that Ventures is contractually barred from having "any control or input over the litigation decisions" for this case. Dkt. 136-1 at 10. The court is not persuaded that further discovery on this matter would bear on any of the claims or defenses or otherwise undermine the already-produced funding agreement. The cases defendants rely upon do not offer much help on this point, as they concern fee and retainer agreements between named parties and their lawyers, not non-party litigation funding agreements. *See Dixon v. Jefferson Capital Sys., LLC*, No. 19-cv-02457, 2020 WL 9607902 (S.D. Ind. Nov. 23, 2020); *Norem v. Lincoln Benefit Life Co.*, No. 10 C 02233, 2011 WL 13555176 (N.D. Ill. June 14, 2011); *Epstein v. Am. Rsrv. Corp.*, No. 79 C 4767, 1985 WL 2598 (N.D. Ill. Sept. 18, 1985). Moreover, plaintiffs are represented by other additional law firms, which are not party to the Ventures funding agreement. Dkt. 134 at 12; *see also* Dkt. 136-3 at 3 (excerpting the agreement between the law firm and Ventures).

Because the requested information is irrelevant to the claims, defenses, and class certification in this case, the court DENIES the portion of defendants' motion related to plaintiffs' law firm's funding arrangements.

B. Factual Bases for Plaintiffs' Allegations

Defendants seek information about the factual bases for plaintiffs' allegations and theories of anticompetitive conduct. Dkt. 117 at 6. The dispute concerning these topics is less about the subject matter of the requests and more about their numerosity. Specifically, defendants have collectively served forty-three interrogatories, and plaintiffs say that exceeds the limit.

Defendants argue that Federal Rule of Civil Procedure 33 entitles each party, not each side, to twenty-five interrogatories, and so the forty-three interrogatories they have served are well within the limit of fifty to which they are collectively entitled. *Id.* at 18. Defendants contend they are not "acting in unison" because the interrogatories served by each party seek information specific to each parties' alleged practices. *Id.* at 19. Alternatively, defendants request leave of the court to serve additional interrogatories in excess of Rule 33's twenty-five-interrogatory limit. *Id.* Defendants argue additional interrogatories are relevant to the claims and proportional to the needs of this large, complex case. *Id.* at 20.

Plaintiffs raise several objections. They primarily argue that courts routinely treat separate parties as one party for the purpose of assessing Rule 33's restrictions when, as here, the parties are represented by the same counsel, act in unison, and seek information for use by both defendants. Dkt. 134 at 16–17 (citing *Council of Blind Metro. Chicago v. City of Chicago*, No. 19-cv-6322, 2021 WL 5140475, at *1 (N.D. Ill. Nov. 4, 2021)). Next, they alternatively argue that defendants' request to expand Rule 33's limit should be denied as untimely because defendants moved the court after the agreed-upon deadline to serve interrogatories. *Id.* at 18–19. Plaintiffs contend that granting leave now will prejudicially burden them. *Id.* at 19. Finally, plaintiffs argue that, even if the court finds the request timely, it should still deny it because the interrogatories are duplicative, overbroad, premature, impermissibly seeking expert opinion, and unsupported by a showing of particularized need. *Id.* at 20–22.

***3** The court addresses each argument, beginning by dispensing with the various non-Rule 33 objections. *Id.* First, the requests are not untimely because, as plaintiffs concede, *id.* at 19, defendants served the interrogatories on the July 12 deadline, and the subsequent filing of this motion does not undermine defendants' procedural compliance. In fact,

plaintiffs acknowledge that the parties were meeting and conferring after July 12 but before the motion was filed, *id.*, which is proper and expected. Fed. R. Civ. P. 37(a)(1). Defendants' motion is not premature either. "Substantial discovery has taken place" over the last eighteen months, *In re H&R Block Mrtg. Corp., Prescreening Litig.*, 2006 WL 3692431, at *4 (N.D. Ind. Dec. 13, 2006), and plaintiffs should be in a position to provide fulsome responses at this point. Finally, the court finds that the requests generally seek relevant information and are neither impermissibly overbroad nor duplicative despite some overlap with previously served interrogatories and their broad scope. The court does see how some of the interrogatories may touch on expert opinion, but for those requests, plaintiffs need only respond to the best of their abilities before expert reports are due and then supplement their responses after the deadline for expert disclosures.

Moving on, the court does not see Rule 33 as a barrier to the propounded interrogatories. Rule 33(a)(1) states that "a party" may serve no more than twenty-five interrogatories. If this per-party default was unacceptable, the parties could have specified a per-side rule in their Rule 26(f) report, like they did for requests for admissions. Dkt. 32 at 12–13. Instead, their Rule 26(f) report defers possible expansion of Rule 33's limits but does not explicitly interpret the rule to apply to each side as opposed to each party. *Id.*

Regardless, even if the default rule did not apply, the court finds that the scope and complexity of this case warrants more expansive discovery than typical.[4] This is a putative class action alleging multiple theories of federal antitrust violations, involving multiple plaintiffs and defendants, and engaging dozens of lawyers. Discovery has been ongoing for almost two years and is open for another six months. *See* Dkts. 35 & 115 (setting the initial schedule and amending to the current schedule). The scope of the third-party discovery alone persuades the court that additional interrogatories beyond the typical twenty-five limit is not unreasonable.

The caselaw on which plaintiffs rely affirms that a court's decision to group parties together is permissive and "committed to the broad discretion of the court." *Am. Council of Blind of Metro. Chicago*, 2021 WL 5140475, at *1 (N.D. Ill. Nov. 4, 2021). Given the nature of this case and the sufficient time remaining for plaintiffs to respond to defendants' requests, the court GRANTS the portion of the defendants' motion seeking responses to their second sets of interrogatories. Plaintiffs must answer the second sets within thirty days of the court's order.

For fairness, the court will expand plaintiffs' collective limit to forty-three interrogatories as well and grants them one week from this order to serve them. If the parties find they need more interrogatories as the case continues, they should meet and confer and resolve the issue with the above points in mind.

C. Boundaries of Geographic and Product Markets

Finally, defendants served one hundred forty-five requests for admission seeking information regarding the boundaries of the relevant geographic and product markets that plaintiffs pled in their complaint. Dkt. 117 at 21. Defendants assert the complaint is unclear, for example, as to the boundaries of the North-Central Wisconsin geographic market, and that their requests would "narrow the issues in dispute for Plaintiffs' proposed relevant geographic and product markets." *Id.* at 21–22.

Plaintiffs object to the requests on multiple grounds. As a threshold matter, plaintiffs note that the parties agreed to limit any substantive requests to thirty "per side," Dkt. 32 at 12, and that defendants are collectively well over that limit. Dkt. 134 at 23. Plaintiffs also argue that defendants are being impatient because proving markets requires expert testimony, *id.*, and the parties already agreed via a stipulation that all expert work product was not discoverable until expert disclosures were due, Dkt. 45.

***4** Regarding the threshold issue, the parties' Rule 26(f) report is clear: "The parties agree that a maximum of 30 requests for admission ... should be permitted per side[.]" Dkt. 32 at 12. That stipulation alone is sufficient to convince the court that compelling answers to more than one-hundred additional requests for admission is inappropriate. But beyond that, proving the relevant markets as a factual matter requires expert testimony, *Vasquez v. Indiana Univ. Health, Inc.*, 40 F.4th 582, 584 (7th Cir. 2022), and the parties unequivocally agreed to prohibit discovery of expert-witness work product or communications at this time, Dkt. 45 at 2.

Defendants' arguments do not refute any of these conclusions. The cases they cite are not antitrust cases; nor do they appear to involve the kind of preclusive expert stipulation in force in this case. Further, the court is skeptical of defendants' concern that waiting until the disclosure of expert discovery will "sandbag" them. Dkt. 117 at 23. Both sides have had

access to the same factual information and so are equally positioned to begin conducting expert analysis and drawing conclusions.

For these reasons, defendants' motion seeking responses to their additional requests for admissions is DENIED.

ORDER

IT IS ORDERED that:

1. Defendants' motion to compel production, Dkt. 116, is GRANTED in part and DENIED in part as specified above.

2. Plaintiffs must serve responses to defendants' second set of interrogatories, nos. 1–4, 6, 7, and 11–22, within thirty days of this order.

All Citations

Slip Copy, 2024 WL 5076039

Footnotes

1 Defendants' interrogatories nos. 2 and 4. Dkt. 119-1 at 11.

2 Defendants' interrogatories nos. 1–4, 6, 7, and 11–22. Dkt. 119-11 & 119-12.

3 Defendants' requests for production nos. 1–145. Dkt. 119-14.

4 As defendants cite in their brief, the court has acknowledged this case is "on a whole different order of magnitude than most cases." Dkt. 74, Hr'g Tr. at 27:6–9 (Jan. 24, 2024).

End of Document

West's Wisconsin Statutes Annotated
Civil Procedure (Ch. 799 to 847)
Chapter 804. Civil Procedure--Depositions and Discovery (Refs & Annos)

W.S.A. 804.01

804.01. General provisions governing discovery

Currentness

(1) Discovery methods. Parties may obtain discovery by one or more of the following methods: depositions upon oral examination or written questions; written interrogatories; production of documents or things or permission to enter upon land or other property, for inspection and other purposes; physical and mental examinations; and requests for admission. Unless the court orders otherwise under sub. (3), and except as provided in ss. 804.015, 804.045, 804.08(1)(am), and 804.09, the frequency of use of these methods is not limited.

(2) Scope of discovery. Unless otherwise limited by order of the court in accordance with the provisions of this chapter, the scope of discovery is as follows:

(a) *In general*. Parties may obtain discovery regarding any nonprivileged matter that is relevant to any party's claim or defense and proportional to the needs of the case, considering the importance of the issues at stake in the action, the amount in controversy, the parties' relative access to relevant information, the parties' resources, the importance of the discovery in resolving the issues, and whether the burden or expense of the proposed discovery outweighs its likely benefit. Information within this scope of discovery need not be admissible in evidence to be discoverable.

(am) *Limitations*. Upon the motion of any party, the court shall limit the frequency or extent of discovery if it determines that one of the following applies:

1. The discovery sought is cumulative or duplicative, or can be obtained from some other source that is more convenient, less burdensome, or less expensive.

2. The burden or expense of the proposed discovery outweighs its likely benefit or is not proportional to the claims and defenses at issue considering the needs of the case, the amount in controversy, the parties' resources, the complexity and importance of the issues at stake in the action, and the importance of discovery in resolving the issues.

(b) *Insurance agreements.* A party may obtain discovery of the existence and contents of any insurance agreement under which any person carrying on an insurance business may be liable to satisfy part or all of a judgment which may be entered in the action or to indemnify or reimburse for payments made to satisfy the judgment. Information concerning the insurance agreement is not by reason of disclosure admissible in evidence at trial.

(bg) *Third party agreements*. Except as otherwise stipulated or ordered by the court, a party shall, without awaiting a discovery request, provide to the other parties any agreement under which any person, other than an attorney permitted to charge a

contingent fee representing a party, has a right to receive compensation that is contingent on and sourced from any proceeds of the civil action, by settlement, judgment, or otherwise.

(c) *Trial preparation: materials.* 1. Subject to par. (d) a party may obtain discovery of documents and tangible things otherwise discoverable under par. (a) and prepared in anticipation of litigation or for trial by or for another party or by or for that other party's representative (including an attorney, consultant, surety, indemnitor, insurer, or agent) only upon a showing that the party seeking discovery has substantial need of the materials in the preparation of the case and that the party seeking discovery is unable without undue hardship to obtain the substantial equivalent of the materials by other means. In ordering discovery of such materials when the required showing has been made, the court shall protect against disclosure of the mental impressions, conclusions, opinions, or legal theories of an attorney or other representative of a party concerning the litigation. This protection is forfeited as to any material disclosed inadvertently in circumstances in which, if the material were a lawyer-client communication, the disclosure would constitute a forfeiture under s. 905.03(5). This protection is waived as to any material disclosed by the party or the party's representative if the disclosure is not inadvertent.

2. A party may obtain without the required showing a statement concerning the action or its subject matter previously made by that party. Upon request, a person not a party may obtain without the required showing a statement concerning the action or its subject matter previously made by that person. If the request is refused, the person may move for a court order. Section 804.12(1)(c) applies to the award of expenses incurred in relation to the motion. For purposes of this paragraph, a statement previously made is a written statement signed or otherwise adopted or approved by the person making it, or a stenographic, mechanical, electrical, or other recording, or a transcription thereof, which is a substantially verbatim recital of an oral statement by the person making it and contemporaneously recorded.

(d) *Trial preparation: experts.* Discovery of facts known and opinions held by experts, otherwise discoverable under par. (a) and acquired or developed in anticipation of litigation or for trial, may be obtained as follows:

1. A party may through written interrogatories require any other party to identify each person whom the other party expects to call as an expert witness at trial. A party may depose any person who has been identified as an expert whose opinions may be presented at trial. Upon motion, the court may order further discovery by other means, subject to such restrictions as to scope and such provisions, pursuant to subd. 3. concerning fees and expenses as the court considers appropriate.

2. A party may, through written interrogatories or by deposition, discover facts known or opinions held by an expert who has been retained or specially employed by another party in anticipation of litigation or preparation for trial and who is not expected to be called as a witness at trial only upon motion showing that exceptional circumstances exist under which it is impracticable for the party seeking discovery to obtain facts or opinions on the same subject by other means.

3. Unless manifest injustice would result, the court shall require that the party seeking discovery pay the expert a reasonable fee for the time spent in responding to discovery under the last sentence of subds. 1 and 2.; and with respect to discovery obtained under the last sentence of subd. 1., the court may require, and with respect to discovery obtained under subd. 2., the court shall require, the party seeking discovery to pay the other party a fair portion of the fees and expenses reasonably incurred by the latter party in obtaining facts and opinions from the expert.

(e) *Specific limitations on discovery of electronically stored information.*

1g. A party is not required to provide discovery of any of the following categories of electronically stored information absent a showing by the moving party of substantial need and good cause, subject to a proportionality assessment under par. (am)2.:

a. Data that cannot be retrieved without substantial additional programming or without transforming it into another form before search and retrieval can be achieved.

b. Backup data that are substantially duplicative of data that are more accessible elsewhere.

c. Legacy data remaining from obsolete systems that are unintelligible on successor systems.

d. Any other data that are not available to the producing party in the ordinary course of business and that the party identifies as not reasonably accessible because of undue burden or cost. In response to a motion to compel discovery or for a protective order, the party from whom discovery is sought is required to show that the information is not reasonably accessible because of undue burden or cost. If that showing is made, the court may order discovery from such sources only if the requesting party shows good cause, considering the limitations of par. (am). The court may specify conditions for the discovery.

1r. No party may serve a request to produce or inspect under s. 804.09 seeking the discovery of electronically stored information, or respond to an interrogatory under s. 804.08(3) by producing electronically stored information, until after the parties confer regarding all of the following, unless excused by the court:

a. The subjects on which discovery of electronically stored information may be needed, when such discovery should be completed, and whether discovery of electronically stored information shall be conducted in phases or be limited to particular issues.

b. Preservation of electronically stored information pending discovery.

c. The form or forms in which electronically stored information shall be produced.

d. The method for asserting or preserving claims of privilege or of protection of trial-preparation materials, and to what extent, if any, the claims may be asserted after production of electronically stored information.

e. The cost of proposed discovery of electronically stored information and the extent to which such discovery shall be limited, if at all, under sub. (3) (a).

f. In cases involving protracted actions, complex issues, or multiple parties, the utility of the appointment by the court of a referee under s. 805.06 or an expert witness under s. 907.06 to supervise or inform the court on any aspect of the discovery of electronically stored information.

2. If a party fails or refuses to confer as required by subd. 1r., any party may move the court for relief under s. 804.12(1).

3. If after conferring as required by subd. 1r., any party objects to any proposed request for discovery of electronically stored information or objects to any response under s. 804.08(3) proposing the production of electronically stored information, the objecting party may move the court for an appropriate order under sub. (3).

(3) Protective orders. (a) Upon motion by a party or by the person from whom discovery is sought, and for good cause shown, the court may make any order which justice requires to protect a party or person from annoyance, embarrassment, oppression, or undue burden or expense, including but not limited to one or more of the following:

1. That the discovery not be had;

2. That the discovery may be had only by specifying terms, including time and place or the allocation of expenses, for the disclosure or discovery;

3. That the discovery may be had only by a method of discovery other than that selected by the party seeking discovery;

4. That certain matters not be inquired into, or that the scope of the discovery be limited to certain matters;

5. That discovery be conducted with no one present except persons designated by the court;

6. That a deposition after being sealed be opened only by order of the court;

7. That a trade secret, as defined in s. 134.90(1)(c), or other confidential research, development, or commercial information not be disclosed or be disclosed only in a designated way;

8. That the parties simultaneously file specified documents or information enclosed in sealed envelopes to be opened as directed by the court.

(b) If the motion for a protective order is denied in whole or in part, the court may, on such terms and conditions as are just, order that any party or person provide or permit discovery. Section 804.12(1)(c) applies to the award of expenses incurred in relation to the motion.

(c) Motions under this subsection may be heard as prescribed in s. 807.13.

(4) Sequence and timing of discovery. Unless the parties stipulate or the court upon motion, for the convenience of parties and witnesses and in the interests of justice, orders otherwise, methods of discovery may be used in any sequence and the fact that a party is conducting discovery, whether by deposition or otherwise, shall not operate to delay any other party's discovery.

(5) Supplementation of responses. A party who has responded to a request for discovery with a response that was complete when made is under no duty to supplement the response to include information thereafter acquired, except as follows:

(a) A party is under a duty seasonably to supplement the party's response with respect to any question directly addressed to all of the following:

1. The identity and location of persons having knowledge of discoverable matters.

2. The identity of each person expected to be called as an expert witness at trial.

(b) A party is under a duty seasonably to amend a prior response if the party obtains information upon the basis of which 1. the party knows that the response was incorrect when made, or 2. the party knows that the response though correct when made is no longer true and the circumstances are such that a failure to amend the response is in substance a knowing concealment.

(c) A duty to supplement responses may be imposed by order of the court, agreement of the parties, or at any time prior to trial through new requests for supplementation of prior responses.

(6) Custody of discovery documents. (a) Unless the court in any action orders otherwise, the original copies of all depositions, interrogatories, requests for admission and responses thereto, and other discovery documentation shall be retained by the party who initiated the discovery or that party's attorney.

(b) The original copy of a deposition shall be retained by the attorney sealed as received from the person recording the testimony until the appeal period has expired, or until made a part of the record.

(7) Recovering information inadvertently disclosed. If information inadvertently produced in discovery is subject to a claim of privilege or of protection as trial preparation material, the party making the claim may notify any party that received the information of the claim and the basis for it. After being notified, a party must promptly return, sequester, or destroy the specified information and any copies it has; must not use or disclose the information until the claim is resolved; must take reasonable steps to retrieve the information if the party disclosed it before being notified; and may promptly present the information to the court under seal for a determination of the claim. The producing party must preserve the information until the claim is resolved.

Credits

<<For credits, see Historical Note field.>>

Editors' Notes

JUDICIAL COUNCIL NOTE--2012

Sup. Ct. Order No. 12-03 states that “the Judicial Council Notes to Wis. Stat. § 804.01 (2) (c), 804.01 (7), 805.07 (2) (d), and 905.03 (5) are not adopted, but will be published and may be consulted for guidance in interpreting and applying the rule."

Sub. (2)(c) is amended to make explicit the effect of different kinds of disclosures of trial preparation materials. An inadvertent disclosure of trial preparation materials is akin to an inadvertent disclosure of a communication protected by the lawyer-client privilege. Whether such a disclosure results in a forfeiture of the protection is determined by the

same standards set forth in Wis. Stat. § 905.03(5). A disclosure that is other than inadvertent is treated as a waiver. The distinction between "waiver" and "forfeiture" is discussed in cases such as *State v. Ndina*, 2009 WI 21, ¶¶28-31, 315 Wis. 2d 653.

Sub. (7) is modeled on Fed. R. Civ. P. 26(b)(5)(B), the so-called "clawback" provision of the federal rules. The following Committee Note of the federal Advisory Committee on Civil Rules regarding the 2006 Amendments to the Federal Rules of Civil Procedure (regarding discovery of electronically stored information) is instructive in understanding the scope and purpose of Wisconsin's version:

> The Committee has repeatedly been advised that the risk of privilege waiver, and the work necessary to avoid it, add to the costs and delay of discovery. When the review is of electronically stored information, the risk of waiver, and the time and effort required to avoid it, can increase substantially because of the volume of electronically stored information and the difficulty in ensuring that all information to be produced has in fact been reviewed. Rule 26(b)(5)(A) provides a procedure for a party that has withheld information on the basis of privilege or protection as trial-preparation material to make the claim so that the requesting party can decide whether to contest the claim and the court can resolve the dispute. Rule 26(b)(5)(B) is added to provide a procedure for a party to assert a claim of privilege or trial-preparation material protection after information is produced in discovery in the action and, if the claim is contested, permit any party that received the information to present the matter to the court for resolution.
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> Rule 26(b)(5)(B) does not address whether the privilege or protection that is asserted after production was waived by the production. The courts have developed principles to determine whether, and under what circumstances, waiver results from inadvertent production of privileged or protected information. Rule 26(b)(5)(B) provides a procedure for presenting and addressing these issues. Rule 26(b)(5)(B) works in tandem with Rule 26(f), which is amended to direct the parties to discuss privilege issues in preparing their discovery plan, and which, with amended Rule 16(b), allows the parties to ask the court to include in an order any agreements the parties reach regarding issues of privilege or trial-preparation material protection. Agreements reached under Rule 26(f)(4) and orders including such agreements entered under Rule 16(b)(6) may be considered when a court determines whether a waiver has occurred. Such agreements and orders ordinarily control if they adopt procedures different from those in Rule 26(b)(5)(B).
>
> A party asserting a claim of privilege or protection after production must give notice to the receiving party. That notice should be in writing unless the circumstances preclude it. Such circumstances could include the assertion of the claim during a deposition. The notice should be as specific as possible in identifying the information and stating the basis for the claim. Because the receiving party must decide whether to challenge the claim and may sequester the information and submit it to the court for a ruling on whether the claimed privilege or protection applies and whether it has been waived, the notice should be sufficiently detailed so as to enable the receiving party and the court to understand the basis for the claim and to determine whether waiver has occurred. Courts will continue to examine whether a claim of privilege or protection was made at a reasonable time when delay is part of the waiver determination under the governing law.
>
> After receiving notice, each party that received the information must promptly return, sequester, or destroy the information and any copies it has. The option of sequestering or destroying the information is included in part because the receiving party may have incorporated the information in protected trial-preparation materials. No receiving party may use or disclose the information pending resolution of the privilege claim. The receiving party may present to the court the questions whether the information is privileged or protected as trial-preparation material, and whether the privilege or protection has been waived. If it does so, it must provide the court with the grounds for the privilege or protection specified in the producing party's notice, and serve all parties. In presenting the question, the party may use the content of the information only to the extent permitted by the applicable law of privilege, protection for trial-preparation material, and professional responsibility.

If a party disclosed the information to nonparties before receiving notice of a claim of privilege or protection as trial-preparation material, it must take reasonable steps to retrieve the information and to return it, sequester it until the claim is resolved, or destroy it.

Whether the information is returned or not, the producing party must preserve the information pending the court's ruling on whether the claim of privilege or of protection is properly asserted and whether it was waived. As with claims made under Rule 26(b)(5)(A), there may be no ruling if the other parties do not contest the claim.

SUPREME COURT NOTE--2010

Sub. (2) (e) was created as a measure to manage the costs of the discovery of electronically stored information. If the parties confer before embarking on such discovery, they may reduce the ultimate cost.

The rule does not require parties to confer before commencing discovery under ss. 804.05 (Depositions upon oral examination), 804.06 (Depositions upon written questions), 804.08 (Interrogatories to parties); or 804.11 (Requests for admission). These discovery devices, if employed before serving a request for production or inspection of electronically stored information, may lead to more informed conferences about the potential scope of such discovery.

Parties may not be able to reach consensus on how discovery of electronically stored information is to be managed. Accordingly, subs. (e) 2. and (e) 3. confer authority on the court to intervene as appropriate. In determining whether to issue an order relating to discovery of electronically stored information, the circuit court may compare the costs and potential benefits of discovery. *See Vincent & Vincent, Inc. v. Spacek,* 102 Wis. 2d 266, 306 N.W.2d 85 (Ct. App. 1981). It is also appropriate to consider the factors specified in the Advisory Committee notes to Fed. R. Civ. P. 26(b)(2)(B): (1) the specificity of the discovery request; (2) the quantity of information available from other and more easily accessed sources; (3) the failure to produce relevant information that seems likely to have existed but is no longer available on more easily accessed sources; (4) the likelihood of finding relevant, responsive information that cannot be obtained from other, more easily accessed sources; (5) predictions as to the importance and usefulness of the further information; (6) the importance of the issues at stake in the litigation; and (7) the parties' resources.

JUDICIAL COUNCIL NOTE--1995

The revision to sub. (2)(d)1. makes it unnecessary to obtain a court order to take an expert's deposition. By mutual agreement, practitioners commonly agree to take experts' depositions without troubling the court for an order. The court's power to control the discovery process is sufficient to prevent abuses. The revision is based on Rule 26(b)(4)(A), F.R.C.P.

Subsection (2)(d)2. is amended to specify that discovery of non-testifying experts may be made by interrogatories or depositions. The revision is based on Rule 26(b)(4)(B), F.R.C.P.

JUDICIAL COUNCIL NOTE--1988

Sub. (3) (c) [created] allows motions for protective orders to be heard by telephone conference. [Re Order effective Jan. 1, 1988]

JUDICIAL COUNCIL NOTE--1986

Sub. (6) requires that the originals of discovery documents be retained by the party who initiated the discovery, or his or her attorney, unless the court otherwise directs, until the time for appeal has expired. [Re Order eff. 7-1-86.]

Notes of Decisions (257)

W. S. A. 804.01, WI ST 804.01
Current through 2023 Act 272, published April 10, 2024.

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