ILFA | INTERNATIONAL LEGAL FINANCE ASSOCIATION

Statement for the Record
International Legal Finance Association

United States House of Representatives
Committee on Oversight and Accountability
September 13, 2023

The International Legal Finance Association ("ILFA") respectfully submits this written statement for the record to the U.S. House Committee on Oversight and Accountability. Founded in September 2020, ILFA, the only representative of the commercial legal finance industry, is a non-profit trade association that promotes the highest standards of operation and service for the industry[1].

Commercial legal finance is a beneficial financing tool for businesses of all sizes, from startups to Fortune 100 companies. That being said, many funded commercial cases are "David vs. Goliath" in nature. Without commercial funding, many meritorious lawsuits would not go forward due to the lack of funds necessary to proceed. It enables parties with meritorious claims to access our justice system, which in turn ensures courts will hear the best legal arguments and arrive at the right legal conclusions. The result is the development of better legal jurisprudence – a benefit to our legal system and to the rule of the law.

Users of this type of capital are law firms and sophisticated commercial actors who are represented by experienced legal counsel and is used for high value commercial disputes, such as breach of contract or antitrust claims, typically with damages at issue in the tens of millions of dollars. The capital is non-recourse, meaning the legal finance provider receives nothing if a case is lost, which necessarily dictates that legal finance providers only invest in the most meritorious of cases, and funding agreements are necessarily case specific, heavily negotiated, and involve in-depth due diligence.

Commercial legal finance providers make passive outside investments, meaning that funders do not control the matters in which they invest. A recipient of legal finance maintains full control over the conduct of the case, including strategy and ultimate decision-making. As such, a legal finance provider's involvement is limited to careful evaluation of the merits prior to the investment, and ancillary advice on identifying expert witnesses or providing counsel based on past experience. Funders also do not disclose case information to investors, eliminating the unfounded and reckless national security concerns of which the Chamber of Commerce complains.

[1] This is entirely separate and distinct from consumer litigation funding, wherein small dollar advances are provided to consumers in connection with pending personal injury and similar types of claims. Pro-regulation critics often purposely conflate the two in an effort to confuse issues.

Commercial legal finance providers are regulated like any other financial service such as services offered by banks, investment firms, and private investors. In particular, some legal finance providers are publicly-traded companies that must comply with global financial market regulations. However, unlike other financial services providers, funders are bound by voluntary professional codes of conduct, such as that promulgated by ILFA, which requires members to uphold the highest standards of best practices, and the Association of Litigation Funders of England and Wales ("ALF"), as well as rules governing courts and other tribunals and rules of professional responsibility governing the practice of law. Those rules ensure that clients maintain control of their cases and that their attorneys do not breach their duties of loyalty and confidentiality to their respective clients.

Insofar as corporate wrongdoers and their insurance companies have pointed to higher verdict amounts as evidence of "social inflation," those cases have little to do with the sorts of matters impacted by commercial legal finance. Moreover, commercial legal finance providers conduct rigorous underwriting before investing in cases, and cases undergoing such review are far more likely to result in rational settlements reflecting true value. Likewise, as noted, these investments are non-recourse, so the legal finance provider receives nothing if a case is lost, which necessarily dictates that legal finance providers only invest in the most meritorious of cases.

For over a decade, the Chamber of Commerce has made specious arguments for the automatic forced disclosure of sources of funding in all civil litigation. Most recently, they have asserted entirely speculative allegations that the financing of litigation is a threat to national security. We believe national security is a very serious matter. Those who engage in fearmongering by spreading careless and baseless accusations without any evidence or facts in order to obtain a long-sought and rejected policy agenda are actually subverting our national security interests by diverting resources from the real and critically important security challenges facing the country today.

There are two separate questions here. The first is whether foreign investment from certain countries is unwelcome. The second is whether foreign adversaries can manipulate the US legal industry through investing in legal finance providers. The answer to the second question is unequivocally no. Investors in legal finance companies have no control over investment decisions made by ILFA member companies and investors cannot direct investments in specific cases or portfolios. Nor do investors have the ability to control or influence the provisions of funding agreements, gain access to sensitive case information, or control or influence litigation decisions, including settlement. In addition, under the Federal Rules of Civil Procedure, corporate defendants can protect confidential discovery material from unwarranted disclosure through the issuance of a protective order. For example, Rule 26(c) allows protection from "annoyance, embarrassment, oppression, or undue burden or expense" through a court issued order that specifies the terms and conditions for the discovery process.

Additionally, courts have significant experience in protecting sensitive and confidential information. While it would be a very serious concern if certain trade secrets or other proprietary

information were to be obtained by a foreign adversary, it would also be very concerning for such information to be obtained by an adversary in litigation. We all have confidence in the system to safeguard information as to the latter. ILFA submits that courts are capable of safeguarding against the former as well.

While ILFA does not oppose disclosure requirements in all instances, we believe that any such requirements should be appropriately tailored and consistent with the Federal Rules of Civil Procedure and applicable law. Despite highly politicized efforts to mandate forced automatic disclosure in various forms, careful examination of the topic has yielded a consensus view among neutral organizations – including the Judicial Conference's Advisory Committee on Civil Rules of the Committee on Rules of Practice and Procedure ("Civil Rules Advisory Committee") and others – that existing disclosure mechanisms are adequate for the vast majority of federal cases.

Over the past several years, ILFA and its members have robustly participated in public policy debates related to the commercial legal finance industry. Such efforts include deliberations by the Civil Rules Advisory Committee, the Advisory Committee on Appellate Rules, the Committee the Association of the Bar of the City of New York ("NYCBA"), the Uniform Law Commission ("ULC"), and the U.S. Government Accountability Office ("GAO").

Indeed, federal courts across the country have issued dozens of opinions analyzing disclosure of financing under Rule 26(b)(1), which have yielded an ever-growing body of precedent holding that disclosure is unwarranted absent special circumstances. Moreover, where disclosure is deemed appropriate, certain courts have exercised their inherent authority to implement orders that narrowly limit disclosure in a manner that promotes judicial economy, follows Rule 26's requirements of relevance and proportionality, and respects attorney-client privilege and work-product protection.

Efforts before the Civil Rules Advisory Committee to amend the Federal Rules of Civil Procedure to mandate disclosure have been persistent yet unsuccessful. In 2014, 2015, 2017, 2018, and 2019, 2020 and 2022, the Chamber of Commerce's Institute for Legal Reform lobbied the Civil Rules Advisory Committee to force disclosure of funding arrangements in all civil cases through an amendment of Rule 26(a)(1)(A). After multiple in-depth studies of the topic, including the creation of a subcommittee that undertook discussions across the country to examine the disparate views on the topic at several academic conferences, the Civil Rules Advisory Committee has repeatedly declined to recommend amending Rule 26 to force disclosure.

As the Advisory Committees recognizes, courts already have the ability to disclose funding agreements, when relevant, during the course of discovery and the vast majority of courts and legislatures have rejected similar proposals and efforts by defendants to force disclosure of financing in commercial matters. The Government Accountability Office studied the commercial litigation funding industry and did not recommend regulation. Even where commercial funding has been disclosed, multiple courts have held that evidence of funding cannot be presented to a jury.

There is no need for a discriminatory rule for the legal finance industry and no basis for one litigant to have to disclose their confidential financial arrangements to an opposing party in litigation. That type of disclosure would be highly prejudicial and create an unlevel playing field. Automatic forced disclosure allows opposing parties to weaponize financing to their advantage, which disadvantages a much larger group of businesses and individuals that would choose to use commercial legal finance.

ILFA thanks the Committee for its consideration of the Association's views and for accepting this statement for the hearing record.