Statement of the U.S. Chamber of Commerce Institute for Legal Reform

Before the United States House of Representatives
The Subcommittee on Courts, Intellectual Property, and the Internet

"The U.S. Intellectual Property System and the Impact of Litigation Financed by Third-Party Investors and Foreign Entities"

June 12, 2024

The U.S. Chamber of Commerce Institute for Legal Reform ("ILR") supports federal legislation that would increase the transparency of third-party litigation funding ("TPLF") usage.

As a program of the U.S. Chamber of Commerce (the "Chamber"), ILR's mission is to champion a fair legal system that promotes economic growth and opportunity. The Chamber is the world's largest business federation, representing the interests of millions of businesses of all sizes, sectors and regions, as well as state and local chambers and industry associations, and it is dedicated to promoting, protecting and defending America's free enterprise system.

TPLF is a rapidly growing business model in which non-parties invest in litigation by paying money to a plaintiff or his/her counsel in exchange for a contingent interest in any proceeds from the lawsuit. At present, virtually all TPLF activity in U.S. courts occurs in secrecy because there is no generally applicable statute or rule requiring disclosure.[1] Moreover, to the extent defendants seek this information through ordinary discovery, plaintiffs generally resist strenuously, and courts often do not compel production of the requested information. Thus, the existence of TPLF in a particular civil action typically becomes known to the court and the parties only if there is compliance with a local rule or standing order requiring disclosure (or a public dispute emerges between the plaintiff and the funder).

Despite this secrecy, it is clear that the amount of litigation being funded by non-party investors has grown by leaps and bounds over the last decade. According to one industry report, during 2023, litigation funders had $15.2 billion in assets

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[1] *See* James Anderson, *Is Increased Transparency into Litigation Financing on the Horizon?*, National Law Review (Jan. 15, 2020), https://www.natlawreview.com/article/increased-transparency-litigation-financing-horizon.

allocated to U.S. commercial investments.[2] Of most relevance to today's hearing, these third-party litigation funders have zeroed in on patent litigation. An analysis conducted in 2022 by Texas A&M University shows that from 2015-2021, at minimum, almost 25% of patent lawsuits in the US were funded by third parties.[3] The same data show that from 2000-2021, Non-Practicing Entities ("NPEs"), persons who hold patents for litigation (not commercial) exploitation purposes, initiated almost half of all patent cases. In addition, at least one 2022 source has stated that "at minimum, almost 25% of all U.S. patent cases are financed by third parties" and that "[e]stimates also show that somewhere between 50% and 60% of all patent litigation involves [NPEs]."[4]

While much of the public attention to TPLF has focused on the patent space, litigation investors have increasingly become entrenched in other aspects of our civil justice system, including the mass torts arena.[5] Flush with cash, plaintiffs' lawyers and their investors are able to work with claim aggregators (also known as lead generators) to drum up clients and claims. "Advertising is the main method to find claimants, and it's handled by an ecosystem of lawyer-specific ad agencies . . . ."[6] These companies engage in aggressive marketing and sell the names of potential claimants to plaintiffs' counsel.[7] Millions of dollars have been spent on such efforts to fuel litigation involving a wide array of topics, including talcum powder, military

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[2] The Westfleet Insider, 2023 Litigation Finance Market Report, available at https://www.westfleetadvisors.com/wp-content/uploads/2024/03/WestfleetInsider2023-Litigation-Finance-Market-Report.pdf.

[3] https://news.bloomberglaw.com/us-law-week/ip-litigation-financing-protects-investors-not-inventors.

[4] Michael B. Mukasey, *Patent Litigation Is a Matter of National Security*, Wall St. J. (Sept. 11, 2022), https://www.wsj.com/articles/patent-litigation-is-a-matter-of-national-security-chips-and-science-act-intellectual-property-theft-lawsuit-technology-scammers-manufacturing-11662912581.

[5] *See* Ronen Avraham, Lynn A. Baker, and Anthony J. Sebok, *The MDL Revolution and Consumer Legal Funding*, 40 Rev. of Lit. 143, 143 (2021) ("mass tort claims pending in [multi-district litigations] constitute the fastest growing sector of those seeking assistance" from third-party litigation funders); *see also* Maya Steinitz, *Follow the Money? A Proposed Approach for Disclosure of Litigation Finance Agreements*, 53 U.C. Davis L. Rev. 1073, 1075 (2019) ("This market in legal claims has attracted . . . private equity [and] hedge funds . . . looking for high-risk high-reward investments . . . .").

[6] Roy Strom, *Camp Lejeune Ads Surge Amid "Wild West" of Legal Finance*, Tech, Bloomberg Law (Jan. 30, 2023), https://www.reuters.com/legal/litigation/jury-says-3m-owes-50-mln-us-army-veteran-latest-earplug-trial-2022-03-25 (such investors "view mass torts as an increasingly lucrative asset class, and are likely to bet even more money on similar cases to diversify their holdings").

[7] *Id.*

ear plugs, baby formula and weedkillers.[8] For example, litigation funding and aggressive advertising on television, radio and social media effectively turned the 3M Combat Arms Earplug litigation into the largest mass tort in U.S. history, generating close to 300,000 claimants.[9] As one member of the plaintiffs' bar put it, "[f]ive or seven years ago, a tort like 3M would have been 50,000 claimants . . . . Now, it's [more than] 275,000 claimants because of innovations around digital marketing and origination, the technology to absorb that type of volume, and capital."[10] Because hearing loss and tinnitus have many causes and become increasingly common with advancing age,[11] plaintiffs' lawyers were able to use media advertising and litigation funding to help amass a large volume of claims and exert enormous settlement pressure on the defendant.

The ubiquity of TPLF in our legal system has also spawned concerns about whether foreign actors are using this clandestine business model to invest in the U.S. civil justice system. Because of the lack of transparency, it is impossible to pinpoint the extent of such foreign investment. This type of funding is undoubtedly occurring, however, as sovereign wealth funds ("SWFs"), state-owned and operated investment funds, are becoming increasingly involved in TPLF.[12] For example, Burford Capital ("Burford") has partnered with an undisclosed SWF since at least 2018 and recently extended this partnership through 2023.[13] Another prominent funder, Therium, also has a relationship with an undisclosed SWF.[14] And we also know that PurpleVine IP, a China-based company that touts itself as a provider of one-stop patent solutions, is funding at least four patent cases in the U.S. against Samsung Electronics and a

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[8] *Id.*

[9] *See, e.g.*, Nate Raymond, *3M Owes $58 Million to Two Veterans in Latest Combat Earplug Trials*, Reuters (Mar. 26, 2022), https://www.reuters.com/legal/litigation/jury-says-3m-owes-50-mln-us-army-veteran-latest-earplug-trial-2022-03-25; Informational Brief of Aearo Techs. LLC at 38, *In re Aearo Techs. LLC*, No. 22-02890-JJG-11, ECF No. 12 (S.D. Ind. July 26, 2022) ("Aearo Informational Brief").

[10] Strom, *supra* note 7.

[11] National Institute on Deafness and Other Communications Disorders, Tinnitus, available at https://www.nidcd.nih.gov/health/tinnitus

[12] https://www.gao.gov/assets/gao-23-105210.pdf., at 10 & n.24.

[13] *See* https://www.burfordcapital.com/shareholders/announcements-container/burford-extends-life-of-sovereign-wealth-fund-arrangement-and-comments-on-fund-management-business/.

[14] https://www.law.com/americanlawyer/2019/03/25/therium-announces-430m-fund-pushing-investments-past-1-billion/.

subsidiary.[15] The possibility of foreign adversaries taking advantage of TPLF to compromise American interests injects yet another troubling dimension into pending legal disputes unrelated to the actual merits of the suit.

In light of the increasingly pervasive usage of TPLF, multiple federal district courts and individual judges are recognizing the need to make this secretive practice more transparent. For example, the U.S. District Court for the District of New Jersey has adopted a local rule requiring disclosure of the identity of each investor in a litigation matter (name, address, place of formation), whether the investor's approval is necessary for litigation and settlement decisions, and a description of the nature of the financial interest.[16] And Chief Judge Colm Connolly of the U.S. District Court for the District of Delaware has adopted a standing order applicable to cases on his docket that largely mirrors the District of New Jersey's approach.[17] Because that order only applies to cases pending before that particular judge, a significant number of cases pending in the District of Delaware (including a bevy of patent cases) are presently not subject to any TPLF-specific disclosure requirements.[18]

While these examples of disclosure requirements reflect a growing recognition of the importance of TPLF transparency, they are inadequate to address this national problem. As pointed out in a December 2022 GAO Report, "[t]here is no nationwide requirement to disclose litigation funding agreements to courts or opposing parties in U.S. federal litigation."[19] And to the extent courts have required

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[15] https://news.bloomberglaw.com/business-and-practice/china-firm-funds-us-lawsuits-amid-push-to-disclose-foreign-ties.

[16] *See* D.N.J. L. Civ. R. 7.1.1(a).

[17] *See* Standing Order Regarding Third-Party Litigation Funding Arrangements, https://www.ded.uscourts.gov/sites/ded/files/Standing%20Order%20Regarding%20Third-Party%20Litigation%20Funding.pdf.

[18] The Executive Branch has also recognized the importance of TPLF disclosure. For example, most recently, the chief of the Foreign Agents Registration Act (FARA) Unit at the Department of Justice (DOJ), Evan Turgeon, highlighted the concerns regarding foreign investment in U.S. litigation. He also announced the DOJ's intention to scrutinize foreign litigation funding as well as the activities of sovereign wealth funds that promote the political or policy goals of foreign governments. *See FARA Officials Preview Major Regulatory Changes and Identify New Areas of Focus*, Dec. 6, 2023, https://www.lexology.com/library/detail.aspx?g=06449b32-a4ab-45d1-b623-6c9f157db21c. Similarly, the Securities and Exchange Commission adopted a rule requiring private equity firms to disclose the percentage of their capital targeted for litigation funding. *See* Andrew Ramonas, *SEC Tells Private Equity Firms to Report on Litigation Finance*, Bloomberg Law, May 3, 2023, https://news.bloomberglaw.com/esg/sec-tells-private-equity-firms-to-report-on-litigation-finance.

[19] https://www.gao.gov/assets/gao-23-105210.pdf., at 26.

some form of disclosure, they have taken widely divergent approaches.[20] In particular, courts differ on who must disclose a financial interest, who is entitled to access the disclosed information, what details must be disclosed, and in what kinds of cases disclosure is mandated.

Accordingly, the time has come for a uniform federal statutory disclosure requirement that would make TPLF arrangements more transparent. To be effective, any such legislation should require disclosure of the existence of funding, the identity of the funders, the identity of any foreign funding sources, ***as well as the production of the underlying TPLF agreements***. Absent these most basic disclosures, TPLF will continue to operate sub rosa, hiding potential conflicts of interest and other ethical issues, such as improper fee-splitting between lawyers and non-lawyers. Further, unless TPLF becomes more transparent, courts will continue to be left in the dark about whether an outside entity is steering a plaintiff's litigation and settlement decisions—a dynamic that is highly relevant to settlement negotiations, the adequacy of counsel in class actions and potential cost-shifting obligations. And absent a uniform disclosure rule, there remains a real risk that foreign competitors (indeed, potential adversaries) may be trying to use U.S. courts to undermine U.S. national or economic security.

To lessen these serious risks and for multiple additional reasons, a uniform TPLF disclosure law is essential to the fair, efficient and ethical functioning of U.S. civil litigation.

1) Uncovering Potential National And Economic Security Risks

While TPLF raises a number of serious questions related to our civil justice system, one issue that has only recently begun to receive meaningful attention—and that is a focus of today's hearing—is whether TPLF threatens U.S. national and economic security. As previously discussed, while the secrecy surrounding TPLF has obfuscated the role of foreign investment in the U.S. litigation system, Burford's and Therium's partnerships with SWFs and the investment by China-backed PurpleVine IP in patent litigation against a subsidiary of Samsung definitively shows that this phenomenon is in fact happening. Recent public statements by the head of the DOJ's FARA unit indicate that foreign investment in U.S. litigation may already implicate existing FARA requirements.[21]

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[20] *See id.*

[21] *See* FARA Officials Preview Major Regulatory Changes, *supra* note 18.

More than a decade ago, a leading academic expert on TPLF warned that "the China Investment Corporation (CIC), China's Sovereign Wealth Fund, [could] fund[] a suit against an American company in a sensitive industry such as military technology" and, in the process, "obtain[] highly confidential documents containing proprietary information regarding sensitive technologies from the American defendant-corporation."[22] Sen. John Kennedy (R.-La.) recently echoed this concern in a letter to Chief Justice John Roberts and U.S. Attorney General Merrick Garland, warning that "[m]erely by financing litigation in the United States against influential individuals, corporations, or highly sensitive sectors, a foreign actor can advance its strategic interests in the shadows since few disclosure requirements exist in jurisdictions across our country."[23] For instance, some adversaries may see an opportunity to prolong litigation for economic or competitive reasons. They may even seek to access confidential trade secret information for state purposes.

Some members of the funding industry have insisted that the use of protective orders can safeguard sensitive discovery materials. These are orders issued by courts to restrict who may see confidential documents produced by the parties. But the idea of using protective orders for this purpose ignores the fact that to craft a meaningful protective order, a court and the parties need to know who might access the documents unless prohibited or limited by the order in the first place. Put simply, the "players" need to be identified so the protective order can be customized to protect against potential improper leaks.

A recent investigative piece published by Bloomberg highlights another potential risk—i.e., that foreign actors (including potential adversaries) may use TPLF to evade U.S. sanctions laws. According to that piece, A1 (a subsidiary of a Russian investment company called Alfa Group) has spent about $20 million in ongoing bankruptcy cases in New York and London on behalf of a Russian agency seeking to recover assets that were allegedly embezzled from a Moscow bank. In fact, after three A1 directors were sanctioned in the UK, the three sanctioned directors sold A1 for about $900 to another A1 director who had not been sanctioned. The director who purchased A1, Alexander Fain, admitted in a

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[22] Maya Steinitz, *Whose Claim is This Anyway? Third-Party Litigation Funding*, 95 Minn. L. Rev. 1268, 1270 (2011).

[23] U.S. Senator John Kennedy, *Kennedy urges Roberts, Garland to take action to protect national security from foreign actors meddling in U.S. courts* (Jan. 9, 2022), https://www.kennedy.senate.gov/public/press-releases?ID=1FBC312C-94B8-409B-B0A3-859A9F35B9F5.

bankruptcy proceeding that he purchased A1 because of a "'complicated geopolitical situation' potentially affecting the litigation."[24]

The Bloomberg investigation has already led to questions in Congress, and Deputy Treasury Secretary Wally Adeyemo testified at a Senate hearing that the Treasury Department needs to look into the use of the litigation finance in the U.S. by foreign actors. Adeyemo testified that litigation financing by foreign actors "is an issue we have to look [at], we have to both work on and try and address."[25] The Deputy Secretary went on to note that "[o]ne of the challenges we have, of course, is that these Russian oligarchs have become quite expert at trying to avoid our sanctions . . . [a]nd from what I've seen, [TPLF] is one of the several ways they're trying to do that."

In short, it is clear that foreign actors, including those with ties to regimes that are hostile to the United States, are using TPLF for various purposes. Disclosure of these arrangements is a matter of national security that a uniform federal disclosure requirement would help to address.

2) <u>Ensuring Compliance With Ethical Obligations, Particularly The Avoidance Of Conflicts Of Interest And Inappropriate Fee-Sharing</u>

By identifying persons/entities with a stake in the outcome of the litigation, the contemplated disclosures would allow courts and counsel to ensure compliance with ethical obligations. One of the most important ethical duties of both courts and parties is to avoid conflicts of interest. As one commentator succinctly explained:

> As some [funding] entities are multibillion- and multimillion-dollar publicly traded entities, requiring disclosure of their role will allow judges to determine whether they have a conflict of interest in administering a case. And for privately held [funding] entities, the web of personal relationships judges [or other judicial officers] have

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[24] https://www.bloomberglaw.com/product/blaw/bloomberglawnews/business-and-practice/BNA%200000018e-5d01-da8a-ad8e-5f5bcc7c0001.

[25] https://news.bloomberglaw.com/product/blaw/bloomberglawnews/exp/eyJpZCI6IjAwMDAwMThlLWM4MzYtZDUwZC1hM2NmLWZlMzZhOTk1MDAwMSIsImN0eHQiOiJCVU5XIiwidXVpZCI6ImszQVVuUDNvWjcrazZsN0ZzSVBLbUE9PU9SVVp1VlR4cEF5OHpJMlg4dzNRU0E9PSIsInRpbWUiOiIxNzEyODM3Mzg2MTIyIiwic2lnIjoiQzM0UnYzbGF3NHByb211WTM4NjJralAva0cwPSIsInYiOiIxIn0=?source=newsletter&item=read-text®ion=digest&channel=business-and-practice.

could be impacted as well, leading to unintentional appearances of impropriety.[26]

A prime example of this problem arose during a racketeering suit against Steven Donziger, who had fraudulently helped secure an $18.2 billion judgment against Chevron Corporation on behalf of Ecuadorians allegedly harmed by the company's drilling practices.[27] During a deposition in that proceeding, Donziger was asked to identify the company that had helped finance the underlying suit against Chevron.[28] Upon being ordered to answer the question by the special master assigned to the case, Donziger disclosed that the funder was in fact Burford Capital—one of the largest funders in the world.[29] The special master then disclosed that he was a former co-counsel with the founder of Burford, who at one time sent the special master a brochure about funding one of Burford's cases.[30] The special master also disclosed that he was friends with Burford's former general counsel.[31] The special master did not recuse himself from the racketeering litigation, and the parties did not insist that he do so.[32] Nonetheless, as the special master recognized, the deposition "prove[d] . . . that it is imperative for lawyers to insist that clients disclose who the investors are."[33]

Disclosure may also reduce the likelihood of unethical fee-sharing between lawyers and non-lawyer funders consistent with Model Rule of Professional Responsibility 5.4, which has been adopted by most states. That rule is designed to safeguard the professional independence of attorneys—that is, ensure that a lawyer's fidelity is to his or her client rather than to an outsider whose primary interest is maximizing its interest in the underlying litigation. However, funders sometimes enter into arrangements directly with lawyers rather than the actual party litigant in a manner that runs afoul of Rule 5.4.

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26 Tripp Haston, *The Missing Key to 3d-Party Litigation Funding*, Law360 (Feb. 7, 2017), https://www.law360.com/articles/888716/the-missing-key-to-3rd-party-litigation-funding.

27 Jennifer A. Trusz, *Full Disclosure? Conflicts of Interest Arising from Third-Party Funding in International Commercial Arbitration*, 101 Geo. L.J. 1649, 1650, 1658 (2013).

28 *Id.* at 1650.

29 *Id.*

30 *Id.*

31 *Id.*

32 *Id.*

33 *Id.* (citation omitted).

For example, in *Gbarabe v. Chevron Corp.*,[34] the plaintiffs commenced a putative class action arising out of an explosion on an oil drilling rig off the coast of Nigeria. Under the agreement entered into by the plaintiffs' counsel and the funder, counsel agreed that the funder would be repaid its $1.7 million investment in the case by way of a "success fee" of six times that amount ($10.2 million), to be paid from attorneys' fees—plus 2% of the total amount recovered by the putative class members.[35] The fact that the funder was to be paid as a "success fee" after the collection of attorneys' fees (i.e., on a contingency basis) means this agreement may have directly violated Rule 5.4's prohibition on fee sharing.

These sorts of provisions can blur the line separating lawyers from non-lawyers and undermine the attorney-client relationship that is at the core of our civil justice system. Requiring disclosure of the identity of litigation investors and mandating disclosure of the actual terms of funding agreements would provide courts and parties with information necessary to prevent potential conflicts of interest. In short, a uniform disclosure requirement would promote ethical litigation in U.S. courts.

3) <u>Enabling Assessment Of Who May Exercise Control Or Influence Over Litigation</u>

A uniform federal disclosure requirement would provide courts and parties information about whether TPLF companies are exercising control or influence over litigation. TPLF companies frequently dismiss such concerns by asserting that they do not control litigation strategy. However, the few TPLF agreements that have come to light demonstrate that, unsurprisingly, TPLF entities actually do exercise various forms of control and influence over the litigation matters in which they invest.

For example, in *Boling v. Prospect Funding Holdings, LLC*, the U.S. Court of Appeals for the Sixth Circuit concluded that the terms of the funding agreements involved in that personal injury matter "effectively g[a]ve [the TPLF entity] substantial control over the litigation."[36] In particular, two of the agreements permitted the funder to require the plaintiff to execute documents or pay filing fees

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[34] *Gbarabe v. Chevron Corp.*, No. 14-cv-00173-SI, 2016 U.S. Dist. LEXIS 103594, at *6 (N.D. Cal. Aug. 5, 2016).

[35] Litigation Funding Agreement ("*Gbarabe* Funding Agreement") § 1.1, *Gbarabe v. Chevron Corp.*, No. 14-cv-00173-SI, Dkt. No. 186-4 (Ex. 13) (N.D. Cal. filed Sept. 16, 2016).

[36] 771 F. App'x 562, 579 (6th Cir. 2019).

to protect the funder's interest. Another agreement provided that "[i]f the Proceeds [from settlement] are insufficient to pay the Prospect Ownership Amount in full, [Prospect] shall receive all of the Proceeds."[37] Such a provision undoubtedly influenced the plaintiff's ability to settle his case since he was required to accommodate [the funder's] flat fee, which accrued with interest.[38] And "[a]ll four Agreements limited [the plaintiff's] right to change attorneys without [the funder's] consent, otherwise [plaintiff] would be required to repay [the funder] immediately."[39]

Notably, a report by the American Bar Association's House of Delegates repeatedly recognizes and emphasizes the inherent risk of funder control, warning against such control over the litigation itself and even over expenses associated with the lawsuit.[40] Indeed, even when a funder's efforts to control a plaintiff's case are not overt, the existence of TPLF funding may subordinate the plaintiff's own interests in the resolution of the litigation to the interests of the TPLF investor. Disclosure of the existence of funding, the nature of the funding, and the circumstances surrounding any right of the funder to approve litigation decisions or settlement would simply give courts the necessary information to assess who actually controls a civil action.

More recent cases continue to reinforce this trend. Most notably, Sysco Corporation filed a series of antitrust class actions against various poultry and meat suppliers that it financed with more than $140 million provided by Burford.[41] When Sysco agreed to give its customers a share of its antitrust claims in 2022, however, Burford allegedly objected and required that the funding agreement be changed to give Burford the right to review and reject settlement offers, provided Burford's consent is not "unreasonably withheld."[42] Once Sysco began receiving settlement

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[37] Purchase Agreement ("*Boling* Purchase Agreement") § 6.1, *Boling v. Prospect Funding Holdings, LLC*, No. 1:14-CV-00081-GNS-HBB, Dkt. 1-3 (Ex. C to Compl.) (W.D. Ky. filed June 19, 2014); *see generally Boling v. Prospect Funding Holdings, LLC*, No. 1:14-CV-00081-GNS-HBB, 2017 U.S. Dist. LEXIS 48098 (W.D. Ky. Mar. 30, 2017).

[38] *Boling* Purchase Agreement at 1.

[39] *Boling*, 771 F. App'x at 580.

[40] *See* ABA, *Best Practices for Third-Party Litigation Funding*, at 11, 12, 13, 15 (Aug. 2020), https://www.americanbar.org/content/dam/aba/directories/policy/annual-2020/111a-annual-2020.pdf.

[41] *In re Pork Antitrust Litig.*, MDL 3031, 2024 U.S. Dist. LEXIS 97801, at *5 (D. Minn. June 3, 2024).

[42] *See* Am. Petition to Vacate Arbitration Award ¶ 40, *Sysco Corp. v. Glaz LLC*, No. 1:23-cv-01451 (N.D. Ill. filed Mar. 20, 2023), ECF No. 18.

offers it found to be reasonable, Burford allegedly sought to obstruct further settlement negotiations, believing the amounts to be too low.[43] Burford instituted proceedings to enjoin Sysco from finalizing settlements, and an arbitral panel granted an *ex parte* temporary restraining order in Burford's favor.[44]

These allegations, if true, contradict Burford's repeated public statement that it does ***not*** exercise any control or influence over the lawsuits it finances.[45] But more importantly, they prove precisely why a rule requiring disclosure and production of TPLF agreements in civil litigation is necessary. Indeed, there may be hundreds of plaintiffs in Sysco's position where funders may have the authority to exercise veto power against the will of the plaintiff, which not only raises serious ethical issues, but also threatens to deter reasonable settlement and needlessly prolong litigation. Automatic disclosure of TPLF agreements guards against these significant risks by making the fact of such TPLF investments transparent and subjecting funders' representations of non-control to the adversarial process. In short, it provides a backstop against the type of potential abuse alleged in the *Sysco* case.

Burford and Sysco eventually settled their dispute. Although most of the details of the settlement remain confidential, one aspect that was publicly disclosed is that Sysco agreed to assign its claims to an affiliate of Burford. The fact that Sysco had to assign its claims to a Burford affiliate just to get out of a series of

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43 *See id.* ¶¶ 30-40.

44 *See id.* ¶¶ 41-58.

45 *See, e.g.*, https://www.burfordcapital.com/how-we-work/with-law-firms/ ("We act as passive investors ***and do not control strategy or settlement decision-making***, and our capital is almost always provided as a non-recourse investment, shifting risk from the firm to Burford.") (emphasis added); https://www.burfordcapital.com/insights/insights-container/byline-pli-legal-finance-post-covid/ ("If the matter wins, they can expect a meaningful share of the remaining damages, and if it loses, they keep any capital advanced, locking in a minimum outcome. In both scenarios, ***the company maintains control of its litigation***—and considerably more control over its finances.") (emphasis added); https://www.burfordcapital.com/insights/legal-finance-101/ ("Reported use of legal finance—also called litigation finance or litigation funding—has doubled in recent years, as companies and law firms increasingly recognize the benefits of gaining better control over legal budgets and risk ***without ceding control of litigation decision-making or settlement***") (emphasis added); https://www.burfordcapital.com/insights/insights-container/how-do-law-firms-use-portfolio-finance/ ("the use of legal finance generally does not alter control of decision-making or attorney-client relationships. Burford makes a portfolio deal directly with the firm, but Burford's role is that of a passive investor. Therefore, ***Burford does not control the litigation or settlement strategy and decision-making***, except when agreed to by our client") (emphasis added); https://www.sec.gov/Archives/edgar/data/1714174/000110465920081137/filename1.htm ("Unlike in our legal finance business, where we are ***financing a client who retains decision-making authority in the litigation*** . . . .") (emphasis added).

lawsuits Burford insisted on litigating raises serious questions about the extent of Burford's control and influence over the actions. Indeed, the defendants in the underlying litigation mounted legal challenges to the substitution of the Burford affiliate as a plaintiff.

Notably, earlier this month, U.S. District Judge John Tunheim (D. Minn.) affirmed a magistrate judge's denial of the requested substitution, reasoning that it "threaten[ed] the public policy favoring the settlements of lawsuits."[46] As the court put it, "Sysco and Burford's conduct is precisely the kind of conduct of which courts are wary." The requested substitution "resulted from their attempt to resolve [a] dispute over whether" Sysco (the plaintiff) or Burford (the investor) "should ***control*** this litigation." While Judge Tunheim refused to "approve such conduct," other judges will have no way of even knowing whether such conduct is at play in their cases unless there is a uniform requirement that TPLF arrangements (including their terms) be disclosed as a matter of course.

In short, the limited TPLF arrangements that have become public confirm that litigation investors do in fact exercise control or influence over the cases they finance. A uniform federal disclosure requirement would ensure that plaintiffs and their counsel are calling the shots rather than their financiers, whose paramount interest is maximizing profit.

4) Providing The Court And Parties With Information Highly Relevant To Settlement Efforts

A uniform federal disclosure requirement would facilitate fair and efficient settlements by making sure that all persons or entities that have a direct financial interest in, and can exert influence or control over the case are known.[47] A party that must pay a TPLF entity a percentage of the proceeds of any recovery may be inclined to reject what might otherwise be a fair settlement offer in the hopes of securing a larger sum of money. Indeed, as an executive of a prominent TPLF company has acknowledged, litigation funding "make[s] ***it harder and more***

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[46] *In re Pork Antitrust Litig.*, MDL 3031, 2024 U.S. Dist. LEXIS 97801, at *13 (D. Minn. June 3, 2024).

[47] The absence of any rule requiring identification of TPLF participants in a case is inexplicable because defendants have long been required to disclose "any insurance agreement under which an insurance business may be liable to satisfy all or part of a possible judgment in the action or to indemnify or reimburse for payments made to satisfy the judgment." Fed. R. Civ. P. 26(a)(1)(A)(iv).

expensive to settle cases."[48] This is so because the party may seek extra money to make up at least some of the amount (likely substantial) that will have to be paid to the TPLF entity.

Notably, in the previously summarized *Sysco* case, the plaintiff attempted to resist this pressure, but ultimately chose to assign its claims to a Burford affiliate when the investor insisted that the litigation ***not*** be resolved outside court. While this represents one of the most egregious examples of a litigation investor attempting to exercise veto power over settlement decisions, investors can also undermine settlement efforts by structuring their agreements to maximize their take of the first dollars of any recovery, thereby deterring reasonable settlements.

For example, in the Chevron Ecuador litigation previously discussed, the funding agreement included a "waterfall" repayment provision, which provided for a heightened percentage of recovery on the first dollars of any award.[49] Under the agreement, Burford would receive approximately 5.5% of any award, or about $55 million, on any amount starting at $1 billion. However, if the plaintiffs settled for less than $1 billion, the investor's percentage would actually go up.

Other agreements that have come to light—including in the patent context—have confirmed this business model. One agreement that (perhaps inadvertently) became public was entered into by Gamon Plus, Inc. and the TPLF funder Gerchen Keller Capital ("Gerchen Keller") in or around February 2016.[50] Under that agreement, Gerchen Keller was to provide approximately $1.5 million in funding for Gamon's pursuit of patent claims against Campbell Soup, including payment of certain attorney fees. Gerchen Keller was to be paid two times the amount of its initial investment, plus 20% of any additional proceeds gained from the litigation.

While TPLF has made it harder to settle many business-to-business cases and lawsuits in the patent context, its usage in the mass torts arena has had an even more pernicious effect. Indeed, one of the key reasons mass tort cases have paid

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[48] Jacob Gershman, *Lawsuit Funding, Long Hidden in the Shadows, Faces Calls for More Sunlight*, Wall St. J. (Mar. 21, 2018), https://www.wsj.com/articles/lawsuit-funding-long-hidden-in-the-shadows-faces-calls-for-more-sunlight-1521633600 (emphasis added).

[49] *See* Funding Agreement Between Treca Financial Solutions and Claimants, *Chevron Corp. v. Donziger*, No. 11-cv-00691, Dkt. No. 356-2 (S.D.N.Y. filed Nov. 29, 2011).

[50] *See* Funding Agreement Between Gerchen Keller Capital and Gamon Plus Inc. et al. (Feb. 2016).

significant dividends for attorneys and their outside investors is that the sheer number of cases filed in a given mass tort litigation imposes enormous pressure on businesses to settle, regardless of the merits of the underlying claims. Because courts have limited resources, "the bigger [a mass torts litigation] gets, the less individualized scrutiny each claim will realistically receive, creating incentives for ever more claims to be filed," and exerting significant pressure on defendants to settle cases.[51]

Nowhere has this dynamic been clearer than in the 3M Combat Arms litigation. As has been suggested by the overseeing court and others, litigation funders invested considerable money in that controversy, particularly to pay for advertising that would generate claims.[52] Because the military has maintained comprehensive records of earplug issuance, each use of earplugs, and the overall health of each soldier while using the earplugs alleged to be defective, the parties in that federal MDL proceeding were able to undertake a rigorous assessment of a subset of filed claims. In 2021, a random sample of 500 claimants designated as "Wave 1" plaintiffs were required to produce evidence supporting their claims.[53] Of that group, 126 (25.2%) reportedly produced no evidence and dropped out of the case, and nearly 75% of the Wave 1 plaintiffs apparently had no record of ever having used Combat Arms earplugs (65% of whom reported using different hearing protection devices altogether).[54] Of the subset of claimants that had used the earplugs in question, 85% reportedly had "normal hearing" according to the World Health Organization's criteria during the periods they alleged had used the products.[55]

If these statistics are even remotely representative of the broader claims pool, the Combat Arms litigation was rife with baseless lawsuits that clearly were not adequately vetted by counsel before they were filed. Presumably, this was at least in part due to the fact that the litigation funding-driven claimant recruitment efforts were so overwhelmingly successful that some counsel simply did not bother to adequately investigate their claims before filing them. Indeed, that appears to have

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[51] Nora Freeman Engstrom, *The Lessons of Lone Pine*, 129 Yale L.J. 2, 24 n.94, 29, 32 (2019).

[52] *See* Emily Siegel, *3M Lawsuit Investors Ordered to Be Unmasked Amid $6 Billion Deal,* Bloomberg Law (Aug. 30, 2023), https://news.bloomberglaw.com/business-and-practice/3m-lawsuit-investors-ordered-to-be-unmasked-amid-6-billion-deal.

[53] *See* Case Management Order No. 31 (Wave Order #1), *In re 3M Combat Arms Earplug Prods. Liab. Litig.*, No. 3:19md2885, ECF No. 2304 (N.D. Fla. Nov. 22, 2021).

[54] *See* Aearo Informational Brief at 38.

[55] *Id.* at 40.

become a business model for some counsel: Use litigation funding money to generate as many claims as possible, do little to vet or develop those claims, and then wait for settlement money to flow. In the earplug litigation, the huge number of pending claims appears to have had the effect desired by plaintiffs' counsel and their investors, as 3M recently announced a $6 billion deal to resolve more than 260,000 claims in the proceeding.[56]

A uniform federal disclosure requirement would apprise courts and defendants in mass tort cases about which counsel may be using the "use TPLF to attract numerous claims but do no work" business model and whose claims may therefore be highly suspect. As a result, disclosure may discourage use of that unethical approach. But even if it does not, a law mandating production of TPLF arrangements would ensure that defendants and courts in mass tort, patent and other cases are equipped to better calibrate settlement initiatives. Further, transparency would allow courts to structure settlement protocols with greater potential to succeed by, for example, conducting mediations attended by litigation investors with influence or control over settlement decisions.

5) <u>Facilitating Assessment Of Whether Funding Arrangements Violate State-Law Prohibitions</u>

Disclosure would enable courts to determine whether TPLF arrangements are running afoul of state-law prohibitions against champerty—the legal doctrine that bars "someone from funding litigation in which he or she is not a party."[57] Various states prohibit "champerty because such conduct encourages and multiplies litigation."[58] While some states no longer recognize this doctrine, recent state and

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[56] Emily Field, *3M Strikes $6B Deal In Combat Earplug Litigation*, Law360 (Aug. 29, 2023), https://www.law360.com/articles/1715917. The involvement of TPLF in the 3M MDL is just one of many examples of outside investors bankrolling mass tort litigation. Another notable example is the ongoing MDL proceeding in the U.S. District Court for the District of New Jersey involving allegations related to cosmetic talc powder. Public disclosures and reporting indicate that a significant number of the talc lawsuits are being funded by outside investors. *See Johnson & Johnson settlement shows the new stakes in litigation finance*, Financial Times, May 20, 2024, https://www.ft.com/content/abd5bf98-378f-4322-b930-68c9b410e783.

[57] John H. Beisner & Jordan M. Schwartz, *How Litigation Funding Is Bringing Champerty Back To Life*, Law360 (Jan. 20, 2017), https://www.law360.com/articles/882069/how-litigation-funding-is-bringing-champerty-back-to-life.

[58] *Boling*, 771 F. App'x. at 580.

federal court decisions applying several states' laws have given renewed vitality to champerty principles, particularly in the TPLF arena.[59]

For example, in the *Boling* case previously discussed, the fact that the funding agreements at issue gave the investors control over the underlying personal injury litigation led the Sixth Circuit to invalidate those contracts as violating Kentucky's prohibition against champerty and the state's usury laws.[60] The funding agreements contained multiple clauses that ceded control over the underlying litigation from the claimant to the funder, including provisions limiting the plaintiff's right to change attorneys without the funder's consent and requiring the plaintiff to take actions to protect the funder's interest.[61] In holding that these provisions rendered the TPLF agreements champertous under Kentucky law, the Sixth Circuit reasoned that the "conditions raise quite reasonable concerns about whether a plaintiff can truly operate independently in litigation."[62]

TPLF disclosure would ensure that lawsuits being financed by outside parties are not contravening applicable state-law rules with respect to champerty. While the cases discussed above arose out of disputes between the investor and a party receiving the funding after the cases were underway, potential champerty violations should be resolved at the beginning of any lawsuit. Indeed, if a party is being sued pursuant to an illegal (champertous) funding arrangement, both that party and the court have a right to know about the existence of funding and whether an outside funder has control or influence over litigation decisions or settlements to an extent that violates state law. In short, without a disclosure requirement, potential violations of state champerty law would remain concealed from the court.

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[59] *See, e.g.*, *Boling*, 771 F. App'x at 580 (affirming holding that series of litigation funding agreements violated Kentucky's champerty prohibition); *WFIC, LLC v. Labarre*, 148 A.3d 812, 818-19 (Pa. Super. Ct. 2016) (counsel's agreement to pay funder out of his fees was champertous under Pennsylvania law because the investors were unrelated parties lacking a legitimate interest in the lawsuit); *In re DesignLine Corp.*, 565 B.R. 341, 343 (Bankr. W.D.N.C. 2017) (trustee's agreement to "sell" several adversarial proceedings to a litigation funder in order to obtain an advance on litigation expenses invalidated as champertous).

[60] *Boling*, 771 F. App'x at 579.

[61] *Id.* at 580.

[62] *Id.*

6) <u>Providing The Court And Parties With Information Highly Relevant To Class Certification</u>

Disclosure of TPLF arrangements is also highly relevant in purported class actions, particularly in evaluating Fed. R. Civ. P. 23(a)(4)'s adequacy-of-representation requirement. Judge Susan Illston recognized that point in the *Gbarabe* case previously discussed, granting the defendant's motion to compel the disclosure of the funding agreement.[63] As the court explained, the "funding agreement is relevant to the adequacy [of representation] determination [required for class certification] and should be produced to [the] defendant."[64] Class actions already raise significant concerns because the individual members of a putative class have little or no ability to control their own claims. Adding a funder to the equation only increases the risk that litigation decisions fail to take account of the putative class members' best interests. Indeed, the funding agreement in *Gbarabe* demonstrates this point, containing several key provisions that suggest the funder's desire to influence the course of the litigation.

For example, in addition to the funding and repayment provisions previously discussed, the agreement in *Gbarabe* referred to a "Project Plan" for the litigation developed by counsel and the funder with restrictions on counsel deviation, particularly with respect to hiring only identified experts.[65] The agreement specifically barred the lawyers from engaging any co-counsel or experts "without [the funder's] prior written consent."[66] Further, another provision required that counsel "give reasonable notice of and permit [the funder] where reasonably practicable, to attend as an observer at internal meetings, which include meetings with experts, and send an observer to any mediation or hearing relating to the Claim."[67] These sorts of provisions potentially undermine the adequacy of representation required by Fed. R. Civ. P. 23(a)(4) for class actions in federal court, providing another important reason for requiring the disclosure of TPLF, the nature

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63 *Gbarabe*, 2016 U.S. Dist. LEXIS 103594, at *6.

64 *Id.* at *5-6.

65 *Gbarabe* Funding Agreement §§ 1.1, 10.1.

66 *Id.* § 10.1.

67 *Id.* § 10.2.4.

of the financial interest at issue and whether the funder has control over litigation or settlement decisions.[68]

In recognition of the relevance of TPLF to the adequacy element of class certification in particular, the U.S. District Court for the Northern District of California adopted its own TPLF disclosure requirement. That court added to its "Standing Order For All Judges" a provision requiring that "[i]n any proposed class, collective, or representative action, the required disclosure includes any person or entity that is funding the prosecution of any claim or counterclaim."[69] While this rule is a good first step, it is no substitute for a uniform federal disclosure law that applies to ***all*** civil cases and requires the production of the actual funding terms themselves.

7) Making Available Information Highly Relevant To Proportionality And Cost Shifting

The disclosure of TPLF arrangements would also aid courts in deciding questions related to discovery costs and potential sanctions. Rule 26(b)(1) states that the scope of discovery shall be "proportional to the needs of the case, considering . . . ***the parties' resources*** . . . [and] whether the burden or expense of the proposed discovery outweighs its likely benefit."[70] Unlike an average plaintiff, a TPLF entity's business purpose is to raise funds to prosecute and profit from litigation. Thus, the existence of TPLF is relevant to the proportionality element of the scope of discovery. TPLF companies are well-heeled strangers to a case who willingly buy into the litigation hoping to profit from its successful prosecution. For the purposes of the resources element of the proportionality requirement contained in Rule 26(b)(1), any TPLF company that has bought a stake in a case should be considered as part of the "parties' resources." It should not be allowed to hide in the shadows behind a relatively impecunious plaintiff.

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[68] Ultimately, the district court denied certification in *Gbarabe* on several grounds, including adequacy of representation. Although the court did not expressly tie the TPLF agreement to its ruling on adequacy, it did find that plaintiffs' counsel "failed to diligently prosecute this case"—a failure the court suggested may have been linked to their struggle in securing funding early on in the litigation. *See Gbarabe v. Chevron Corp.*, No. 14-cv-00173-SI, 2017 WL 956628, at *7 n.7, *35 (N.D. Cal. Mar. 13, 2017).

[69] Standing Order for all Judges of the Northern District of California, Contents of Joint Case Management Statement, § 19 (Jan. 2017).

[70] Fed. R. Civ. P. 26(b)(1) (emphasis added).

Similarly, because a funder is effectively a real party in interest, it should bear responsibility (to the same degree as any other party) for any wrongdoing in the prosecution of a case and any resulting judicial imposition of sanctions or costs. For example, in *Abu-Ghazaleh v. Chaul*, a Florida state appeals court held that TPLF investors (an individual and company) that controlled the litigation qualified as parties to the lawsuit and therefore became liable for the defendant's attorneys' fees and costs.[71] The state statute at issue in that case specifically authorized the levy of attorneys' fees on the plaintiff where the claim advanced was "without substantial fact or legal support."[72] The court found that the plaintiff's claim was bereft of such legal or factual support. The court then determined that the TPLF investors were liable for the attorneys' fees because they were essentially parties to the litigation (and the named plaintiff was financially unable to pay such fees, which is often the case). The court reached this conclusion by scrutinizing the agreement entered into by the plaintiff and the TPLF investors, which provided that they were to receive 18.33% of any award the plaintiffs received and gave them "final say over any settlement agreements proposed to the plaintiffs."[73] As evidenced by *Abu-Ghazaleh*, if courts are put on notice that a third party is financing the underlying litigation, they will be in a much better position to determine how to impose sanctions or other costs, if such costs are warranted in a given case.

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In sum, the funding arrangements that have become public demonstrate that in some instances, TPLF can inject into civil lawsuits conflicts of interest, unethical fee-sharing, interfere with a plaintiff's control over her lawsuit, frustrate settlement efforts and even potentially undermine national and economic security. The only way to know whether a particular litigation funding arrangement is raising any of these serious concerns is for the existence and terms of the agreement to be disclosed to the other side and the court. Because a uniform federal TPLF disclosure law would do just that, ILR urges that such legislation be enacted as soon as possible.

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[71] *Abu-Ghazaleh v. Chaul*, 36 So. 3d 691, 693-94 (Fla. Dist. Ct. App. 2009).

[72] *Id.* at 694 (citation omitted).

[73] *Id.*