2012

Litigation Finance: What Do Judges Need to Know?

Bert Huang
Columbia Law School, bhuang@law.columbia.edu

Litigation Finance: What Do Judges Need to Know?

BERT I. HUANG*

In any future case in this district such an agreement must be revealed to the court and members of the class as soon as possible. A "sunshine" rule is essential to protect the interests of the public, the class, and the honor of the legal profession.[1]

In our classic image of an American lawsuit, including class actions, the plaintiff's lawyer pays the upfront costs and then hopes to recoup them from a share of the winnings. But today, this picture is incomplete. It is no longer only the law firm's own war chest that finances a case — so can outside investors and lenders.[2] As Judge Hellerstein has just reminded us, the 9/11

* Associate Professor of Law, Columbia Law School. The author thanks Judge Jack Weinstein for the invitation to speak at his conference on mass litigation (this essay grew from his remarks). The author is grateful to our fellow panelists Elizabeth Cabraser, Jack Coffee, Ken Feinberg, Judge Alvin Hellerstein, and Amy Shulman for their reactions. The author also thanks Scott Hemphill, Judge Gerard Lynch, Josh Picker, and Judge Jed Rakoff for their insightful comments. John Briggs and Courtney Heavey offered superb research assistance.

1. *In re* Agent Orange Prod. Liab. Litig., 611 F. Supp. 1452, 1453–54 (E.D.N.Y. 1985), *rev'd*, 818 F.2d 216 (2d Cir. 1987). This was Judge Weinstein's exhortation in a class action which, as he reminds us, was "partially financed through funds advanced by plaintiffs' attorneys who did not perform any legal work." Jack B. Weinstein, *The Democratization of Mass Actions in the Internet Age*, 45 COLUM. J.L. & SOC. PROBS. 451, 468 (2012). The Second Circuit agreed that "in all future class actions counsel must inform the court of the existence of a fee sharing agreement at the time it is formulated." *Agent Orange*, 818 F.2d at 226 (2d Cir. 1987). With the rise of investments in lawsuits by hedge funds, banks, and other outside investors, Judge Weinstein now also urges that "the court should be made aware of any *third-entity* financing arrangements as soon as possible." *Id.* (emphasis added).

2. For recent surveys and analyses, see John C. Coffee, Jr., *Litigation Governance: Taking Accountability Seriously*, 110 COLUM. L. REV. 288, 339–42 (2010); Deborah R. Hensler, *Future of Mass Litigation*, 79 GEO. WASH. L. REV. 306 (2011); Jonathan T. Molot,

cases he presided over involved such third-party financing.[3] The Ecuadorian plaintiffs' environmental case against Chevron, now pending in the Southern District of New York, is another prominent example in the news.[4]

Although such investments are usually confidential, the use of "alternative litigation financing" or "third-party litigation funding" in the United States appears to be growing.[5] Specialty firms are multiplying.[6] Hedge funds and major banks are also getting involved.[7] Credit Suisse, for instance, recently spun off its "litigation risk strategies" division into a standalone litigation financing firm.[8] And Citigroup backed Counsel Financial, the lender in

---

Litigation Finance: A Market Solution to a Procedural Problem, 99 GEO. L.J. 65 (2010); Maya Steinitz, *Whose Claim Is This Anyway? Third-Party Litigation Funding*, 95 MINN. L. REV. 1268 (2011); Steven Garber, *Alternative Litigation Financing in the United States: Issues, Knowns, and Unknowns*, RAND INST. FOR CIV. JUST. (2010), http://www.rand.org/content/dam/rand/pubs/occasional_papers/2010/RAND_OP306.pdf. This essay's focus excludes consumer loans or cash advances to cover a plaintiff's living costs or business expenses while litigation continues.

3. *See* Alvin K. Hellerstein, *Democratization of Mass Tort: Presiding over Mass Tort Litigation to Enhance Participation and Control by the People Whose Claims Are Being Asserted*, 45 COLUM. J.L. SOC. PROBS. 473, 473–75 (2012).

4. *See* Patrick Radden Keefe, *Reversal of Fortune*, THE NEW YORKER, Jan. 9, 2012, at 38, 43 (describing Ecuadorian plaintiffs' third-party funding); Roger Parloff, *Have You Got a Piece of This Lawsuit?*, CNN MONEY (June 28, 2011, 2:06 PM), http://features.blogs.fortune.cnn.com/2011/06/28/have-you-got-a-piece-of-this-lawsuit.

5. *See, e.g.*, Binyamin Appelbaum, *Betting on Justice: Putting Money on Lawsuits, Investors Share in the Payouts*, N.Y. TIMES, Nov. 15, 2010, at A1 (noting that large banks, hedge funds, and investors are looking to lawsuits as new investment vehicles); Paul M. Barrett, *Lawsuit Finance Moves Up the Food Chain*, BLOOMBERG BUSINESSWEEK, Jan. 16, 2012, at 42 (discussing rise of "sophisticated investment outfits" that "specialize in making bets on bigger-dollar cases"); Brandon Pierson, *Ethics Opinion Urges Wariness in Dealing with Lawsuit Funding*, N.Y. L.J., June 16, 2010, at 1 (noting ethical considerations that may accompany the increase in third-party lawsuit funding); Nate Raymond, *Attorneys Explore Third-Party Funding in Commercial Disputes*, N.Y. L.J., June 3, 2010, at 1 (discussing growth of sophisticated third-party funding of commercial litigation); *see also Timeline: Legal Path to Lawsuit Lending*, N.Y. TIMES (Nov. 14, 2010), http://www.nytimes.com/interactive/2010/11/13/business/20101113_lawsuit_timeline.html (charting history of lawsuit funding).

6. *See, e.g.*, Garber, *supra* note 2, at 11 tbl.1, 14 tbl.2, 15 tbl.3 (listing litigation financing firms active in the United States); Hensler, *supra* note 2, at 321 tbl.8 (categorizing "High-End Third-Party Funders").

7. *See, e.g.*, Appelbaum, *supra* note 5 (identifying lawsuit financed by a $3.5 million loan from a New York hedge fund).

8. Jennifer Smith, *Credit Suisse Parts with Litigation Finance Group,* WALL ST. J. L. BLOG (Jan. 9, 2012, 6:13 PM), http://blogs.wsj.com/law/2012/01/09/credit-suisse-parts-with-litigation-finance-group/; Ross Todd, *Credit Suisse Litigation Finance Unit Spins Off to Form Parabellum Capital*, AM. LAWYER, Jan. 10, 2012, http://www.law.com/jsp/tal/PubArticleTAL.jsp?id=1202538125544.

Judge Hellerstein's 9/11 cases.[9] The structure of the financing is also becoming more creative; ideas are crossing over from Great Britain and Australia, where third-party litigation funding has a longer history.[10] A variety of schemes, including some so-called "loans" that are in effect equity stakes in the outcomes of the case, are already in use.

How might such outside financing affect the governance of mass litigation? Consider the familiar worry about potential conflicts of interest between plaintiffs and their attorneys, under typical contingency fee arrangements. To this already difficult problem of ethics and incentives, third-party litigation financing adds a further dimension: it adds (yes) a third party.[11] In academic parlance, it complicates the principal-agent problem by adding a new principal.[12] Most obviously, if banks and hedge funds have interests at stake, they may well want some say in how the litigation is run, or in how and when it ends. And it is easy to imagine other distortions in litigation governance, perhaps affecting the selection of counsel or the choice to bring suit in the first place.

One premise of today's dialogue (as Judge Weinstein's remarks emphasize) is that judges can and should take measures to reduce such distortions or even to resolve the conflicts of interest creating them. This is an especially sensible and widely accepted premise in class actions. Judges are given a formal set of useful

---

9. Appelbaum, *supra* note 5; Kirby Griffis, *Follow the Money: Litigation Funders Back Your Foes*, METRO. CORP. COUNS., July 2011, at 1, 6.

10. *See, e.g.*, Hensler, *supra* note 2, at 320–23 ("Now, third-party litigation investment firms are entering the high end of the litigation market in the United States, spurred on in part by success in Australia and, more recently, England and Western Europe . . . ."); Richard Lloyd, *The New, New Thing*, AM. LAWYER (May 17, 2010), http://www.law.com/jsp/tal/PubArticleTAL.jsp?id=1202457711273 (discussing spread "of third-party litigation funding . . . around the world through Australia, Europe, and now the United States"). *Cf.* David Abrams & Daniel Chen, A Market for Justice (2009) (unpublished manuscript) (on file with the author) (reviewing origins of litigation funding in Australia).

11. *See, e.g.*, Coffee, supra note 2, at 342–43 (discussing principal-agent relationships in third-party litigation funding).

12. For a sampling of the literature on principal-agent problems between attorneys and clients, including in class actions, see, e.g., Bruce Hay & David Rosenberg, *"Sweetheart" and "Blackmail" Settlements in Class Actions: Reality and Remedy*, 75 NOTRE DAME L. REV. 1377 (2000); Samuel Issacharoff, *Class Action Conflicts*, 30 U.C. DAVIS L. REV. 805 (1997); Jonathan R. Macey & Geoffrey P. Miller, *The Plaintiffs' Attorney's Role in Class Action and Derivative Litigation: Economic Analysis and Recommendations for Reform*, 58 U. CHI. L. REV. 1 (1991); A. Mitchell Polinsky & Daniel L. Rubinfeld, *Aligning the Interests of Lawyers and Clients*, 5 AM. L. & ECON. REV. 165 (2003).

tools — and obligations — for addressing conflicting interests in class actions, at least under the federal rules: not only must judges assess the adequacy of representation in deciding whether to certify a class, under Rule 23(a); but they are also tasked with selecting class counsel under Rule 23(g). Moreover, class wide settlements must meet judicial approval, under Rule 23(e), and the terms to be approved include those allocating costs and attorneys' fees. Sharp observers have started to warn that "nontraditional third-party funding for class actions . . . might raise new issues pertaining to adequacy of representation, appointment of class counsel, settlements, and legal fees."[13] In light of Rule 23, such an observation not only points to potential concerns but also reminds us of the safeguards already at hand.

To use such tools most effectively, judges will need to understand how outside financing might press against (or in favor of) the plaintiffs' interests in any given case. And the earlier the financing structure is understood, the better; as the Second Circuit observed, in disapproving the co-counsel financing scheme in the Agent Orange cases:

> [I]n all future class actions counsel must inform the court of the existence of a fee sharing agreement at the time it is formulated. This holding may well diminish many of the dangers posed to the rights of the class. Only by reviewing the agreement prospectively will the district courts be able to prevent potential conflicts from arising, either by disapproving improper agreements or by reshaping them with the assistance of counsel . . . .[14]

What questions, then, should judges be asking when they confront a case involving *third-party* funding? After decades of experience with contingency-fee class actions, the judiciary may have a good grasp of how to identify conflicting interests and other dangers, in that familiar setting. But third-party funding is newer and more complex, involving investors who may have no duty to the class members and whose interests may diverge from those of both counsel and class. Moreover, financing structures vary

13. Hensler, *supra* note 2, at 322.
14. *In re* Agent Orange Prod. Liab. Litig., 818 F.2d 216, 226 (2d Cir. 1987).

along many dimensions; some formats may entail worse risks as a general matter, and even so, the actual distortions (and potential remedies) may yet turn on the specifics of the case.

New lines of questioning are thus needed just to gather the raw factual matter to inform a court's evaluation. These will need to be refined by experience and refreshed over time as financing innovations continue to create new risks. My aim here is only to suggest a starting point for this evolving inquiry.

A. WHAT QUESTIONS SHOULD JUDGES ASK?

Let me first suggest a few basic questions focused on the structure of the financing, on the funder's degree of control over the conduct of litigation, and on how the funding affects asymmetries between the parties. For convenience, I've styled these questions for plaintiff-side funding; but they can be easily recast to apply to financing for the defense side.

The indispensable task is to uncover the precise bounds of the competing incentives created by the financing structure. Thus the first set of questions is aimed at piercing simplistic labels such as "loan" or "investment," in order to reveal the actual structure of the funder's stake in the outcome, and to see how it might create conflicting interests for the funders, the lawyers, and the parties at each stage of the litigation.

1. *Financing Structure*

* Who is funding the litigation? Who arranged the funding? Who has been informed (or not) about the financing terms?

* Does the financing flow to the lawyers or to the clients?[15] Is it financing only a single case at the law firm or a portfolio of the firm's cases?[16]

---

15. Garber, *supra* note 2, at 8 ("[T]here are three main kinds of [litigation funders] currently active . . . : (1) companies that provide consumers with legal funding, (2) companies that lend to plaintiffs' law firms, and (3) companies that invest in commercial (i.e., business-against-business) claims on the plaintiff side."). Some litigation funders might choose to cater to defendants rather than plaintiffs. Steinitz, *supra* note 2, at 1276.

16. *See* Griffis, *supra* note 9, at 6 (noting that plaintiffs' firms can obtain a "single cash advance," "a case cost line of credit," or "an attorney line of credit, which the firm can use for anything it likes," and that a "funding package consisting of an attorney line of credit secured by recovery rights in a firm's whole inventory is rather difficult to distinguish from owning stock in the firm").

* How will the funder be paid? Is it taking interest payments, a share of the recovery, or both? Whose portion of the recovery will be charged for this payment: the lawyers or the parties?

* Does the rate of return or the size of the funder's stake depend on the amount of recovery? Does it depend on whether the remedy is injunctive or monetary?

* What do the funders receive if there is no recovery? If the funding is called a "loan," is it recourse or non-recourse — and how is it secured?[17]

* Does the rate of return or the size of the funder's stake depend on whether the outcome is a judgment or a settlement? Do they depend on which stage of litigation is reached or how long it takes to achieve the outcome?

* What share of the litigation costs is covered by the financing? Is it a fixed amount? If it is a variable amount, what does it depend on?

* Does the funding occur in stages?[18] What criteria determine whether the next stage will be reached? What criteria allow the investor to exit?

* Does the arrangement limit or anticipate further borrowing from or investments by other third parties?[19]

* Is the funder in effect insuring the plaintiff? If so, for what range of losses, with what effective deductibles, and at what effective premiums?[20]

---

17. *Id.* ("The money is secured by the firm's potential rights to recovery ... ranging from the right to recovery in a particular case to the rights in a firm's entire inventory of cases.").

18. *See, e.g.*, Daniel Fisher, *Litigation-Finance Contract Reveals How Investors Back Lawsuits*, FORBES (June 7, 2011, 7:12 AM) (detailing Burford Group's multi-stage financing of the Ecuadorian case against Chevron, with an initial investment of $4 million to be followed by two further "tranches" of $5 million each), http://www.forbes.com/sites/danielfisher/2011/06/07/litigation-finance-contract-reveals-how-investors-back-lawsuits. For further analysis of this contract, see Maya Steinitz, *The Litigation Finance Contract* (Univ. Iowa Legal Studies Research Paper No. 12-11), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2049528.

19. For instance, does it include terms concerning a right of first refusal, or limiting dilution of the present investor's stake?

20. *See, e.g.*, Coffee, *supra* note 2, at 341 (noting one view arguing that funders would be no more invasive than insurance companies already are); Molot, *supra* note 2, at 102–03 (imagining the result of insurance providers being allowed to enter the legal market); Steinitz, *supra* note 2, at 1331–32 (comparing defense funding to after-the-event insurance, but finding that plaintiff funding is analogous to a financing agreement).

* Does the financing arrangement otherwise affect the timing or amount of the lawyers' or the party's compensation?

2. *Influence on the Conduct of Litigation*

* Does the funder have formal control over any litigation decisions?[21]

* Does the funder have de facto influence over litigation decisions — such as through the threat of withdrawing funding, or through conditions on offering funding in the first place?[22]

* Does the funder have the power, formally or de facto, to set settlement terms? Can it influence the acceptance, refusal, or timing of settlements?

* Does the financing alter the counsel's or the party's incentives to settle earlier?[23]

* Has the funder in effect appointed the counsel? If the funder can influence the choice of counsel, does that translate into influence over the counsel's actions?[24]

* Has the funder, or the terms of financing, otherwise narrowed the party's choice of counsel? Or to the contrary, has the availability of funds broadened the choice of counsel?[25]

---

21. *See* Coffee, *supra* note 2, at 340–41 (contrasting Australian funders' practice of "making important litigation decisions" with current United States funders' practice of not interfering); Steinitz, *supra* note 2, at 1279–80 (discussing Australian High Court decisions permitting "third-party funding with the funder having broad powers to control the litigation").

22. *See, e.g.*, UNIV. OF OXFORD, INT'L CONFERENCE ON LITIG. FUNDING 23 (May 19, 2010) (unpublished proceedings) [hereinafter OXFORD CONFERENCE] ("Sensitive situations arise when a funder places improper pressure on a party or lawyer in relation to terms of the arrangement, or in relation to when to accept a settlement or at what level, or decides to withdraw support inappropriately.")

23. For a range of possibilities, see, *e.g.*, Coffee, *supra* note 2, at 342 (arguing that funders would lessen the incentive for contingency-fee attorneys to settle early); Molot, *supra* note 2, at 93–94 (noting potential for high effective interest rates to encourage plaintiffs to settle quickly); Steinitz, *supra* note 2, at 1320 (noting potential for certain financing arrangements to diminish litigants' incentives to pursue their claims or defenses vigorously).

24. *See* OXFORD CONFERENCE, *supra* note 22, at 23 ("If a funder selects the lawyer, this may bring advantages of expertise and lower price, but might also increase potential for improper pressure.").

25. For instance, financing may enable a party to hire counsel at billable rates rather than on a contingency fee. *See* Raymond, *supra* note 5 (quoting attorney Louis Solomon's explanation that third-party funding "has meant clients can hire Mr. Solomon and Cadwalader [on an hourly fee basis] when they might otherwise have needed to engage someone with a different fee structure and not their first choice"). I thank Josh Picker for bringing

3. *Asymmetries Between Parties*

* Does the arrangement treat all plaintiffs under similar terms, or are some subsets favored over others? For instance, are named plaintiffs treated differently from absentees? Are members who actively opt in treated different from those who merely do not opt out?[26]

* Does the financing work to counterbalance the defendant's greater resources?[27] Its greater tolerance for risk? Its greater bargaining power? Or to the contrary, does the financing exacerbate asymmetries that already favor the plaintiffs?[28]

B. WHAT CAN JUDGES DO?

A second group of questions tests the scope of a judge's toolkit in a given case for uncovering, regulating, and potentially even harnessing third-party influences. Which tools are more readily available may vary widely — by cause of action, for instance, or from court to court. Thus, these questions may seem fanciful for some cases, but for others, they may prompt a closer look at how present safeguards can be adapted to new concerns arising from third-party funding.

First comes the matter of uncovering the financing structure. Echoing the Second Circuit's command in the Agent Orange litigation,[29] Judge Weinstein is now urging that "the court should be made aware of any *third-entity* financing arrangements as soon as possible" to allow "the court to better supervise the litigation"

this story to my attention. *See* Joshua Picker, Monitoring the Attorney-Agent: Third-Party Litigation Funding and the Agency Costs of Damages Class Actions (Dec. 20, 2011) (unpublished manuscript) (on file with the author).

26. *See infra* note 45 and accompanying text.

27. *See, e.g.*, Molot, *supra* note 2, at 82–90 (arguing litigation finance would redress bargaining imbalances by countering effects of parties' unequal risk tolerance).

28. In a given case, of course, the plaintiffs' side may have the greater tolerance for risk or the greater bargaining power. *See, e.g.*, John Beisner et al., *Selling Lawsuits, Buying Trouble: Third-Party Litigation Funding in the United States*, U.S. CHAMBER INST. FOR LEGAL REFORM, 8 (Oct. 2009), http://www.instituteforlegalreform.com/sites/default/files/thirdpartylitigationfinancing.pdf (noting that "in the context of aggregate litigation .... third-party funding encourages plaintiffs' attorneys to test claims of questionable merit, knowing that the enormity of the potential risk will often force defendants to settle . . . .").

29. *In re* Agent Orange Prod. Liab. Litig., 818 F.2d 216, 226 (2d Cir. 1987) ("[I]n all future class actions counsel must inform the court of the existence of a fee sharing agreement at the time it is formulated.").

and "to ensure that client interests are not compromised."[30] How might these disclosures be achieved?

1. *Disclosure of Financing*

* How might the court induce a party to disclose the terms of its financing?[31] Or at least to disclose what share of an award or settlement will go to the funders?[32] For instance, can the court direct a party to include such details in a motion for class certification? Or in the settlement notice to class members?

* Where the terms of a financing agreement might reveal the weaknesses or the strategies of the funded party, should such disclosures be made *in camera*?[33]

* Or to the contrary, should opposing counsel be allowed to pose questions about the financing?[34] Can opposing counsel be expected to press the inquiry?[35]

---

30. Weinstein, *supra* note 1, at 470 (emphasis added).

31. One natural starting point is to consider those disclosures contemplated at each of the checkpoints of Federal Rule of Civil Procedure 23. For instance, Rule 23(e) is understood to require "parties seeking approval of a settlement, voluntary dismissal, or compromise under [Rule 23(e)] to file a statement identifying any agreement made in connection with the settlement." FED. R. CIV. P. 23(E) advisory committee's note (referring to the current Rule 23(e)(3)). This requirement aims "at related undertakings that, although seemingly separate, may have influenced the terms of the settlement by trading away possible advantages for the class in return for advantages for others. Doubts should be resolved in favor of identification." *Id.* This has been construed broadly "to encompass such matters as . . . division of fees among counsel" or the revelation of "additional funds that might have been paid to the class that are instead paid to selected claimants or their attorneys." MANUAL FOR COMPLEX LITIGATION (FOURTH) § 21.631 (2004). In some cases, such a "necessarily open-ended" inquiry, *id.*, might be argued to encompass financial obligations to third-party funders.

32. To consider one vivid illustration: In a fee dispute arising from the 9/11 cases, Judge Hellerstein ordered plaintiffs' counsel to absorb $6.1 million in interest payments for their third-party loans, rather than pass those costs through to their clients; he had raised doubts about "how well the clients were informed over the years of the expenses." *See* Mireya Navarro, *Judge Rejects $6.1 Million in 9/11 Case Legal Fees*, N.Y. TIMES, Aug. 27, 2010, at A17.

33. As Judge Weinstein observes, *in camera* disclosure may be appropriate to avoid signaling "financial strain" to opposing parties. Weinstein, *supra* note 1, at 470. At times, of course, other factors may override this consideration. *See, e.g.*, Parloff, *supra* note 4 (describing Judge Lewis Kaplan's order to disclose the details of third-party funding, among other materials, in the Ecuadorian plaintiffs' case against Chevron).

34. That is, if such questions can be walled off from the merits. I thank Judge Rakoff for the insight that (in this regard) defense counsel may well have an informational advantage over the judge. Note that, in theory, such expertise could be useful even if the actual inquiry occurs in camera; one might imagine that defense counsel could be allowed to suggest questions for the judge (but not be privy to the answers).

* How might the use of such methods of disclosure influence the terms of financing in future cases?

2. *Regulation of Influence*

* How might the court take financing structures into account when choosing lead attorneys, such as under Rule 23(g) for federal class actions?[36] Or when choosing lead plaintiffs to monitor the litigation, such as under the Private Securities Litigation Reform Act?[37]

* How might the court take financing structures into account when deciding whether to certify a class action — for instance, in its "adequacy" inquiry under Rule 23(a)(4) for federal class actions? Or when defining the class or the class claims to be certified under Rule 23(c)(1)(B)?

* How might the court take financing structures into account in approving settlements, such as under Rule 23(e) for federal class actions?[38]

* How might the court take the financing structure into account in assigning attorneys' fees and costs?[39]

---

35. Consider, for instance, that "the settlement agreement often contains an express term that defendants will not object to the plaintiffs' lawyers fee application," Jed S. Rakoff, *Are Settlements Sacrosanct?*, 37 LITIG. 15, 16 (Summer 2011).

36. Note that Rule 23 not only permits, but "require[s]" the court to consider "the resources that counsel will commit to representing the class" when appointing class counsel. FED. R. CIV. P. 23(g)(1)(A)(iv). It also permits the court to "consider any other matter pertinent to counsel's ability to fairly and adequately represent the interests of the class," "order potential class counsel to provide information on any subject pertinent to the appointment," and "make further orders in connection with the appointment." FED. R. CIV. P. 23(g)(1)(B), (C), (E).

37. *See* 15 U.S.C. §§ 77z-1(a)(3), 78u-4(a)(3) (2006) (requiring appointment of the "most adequate plaintiff," generally the investor with the greatest financial interest, as lead plaintiff in securities class actions).

38. As Judge Hellerstein has explained, in the context of his handling of the 9/11 cases, it may take more finesse for a judge to demand changes to settlement terms in mass litigations not governed by Rule 23. *See* Hellerstein, *supra* note 3, at 476–77.

39. The judge's expanded role in regulating attorneys' fees in class actions is familiar. *See, e.g.*, MANUAL FOR COMPLEX LITIGATION, *supra* note 31, § 14.2 (offering guidance and citing extensive case law); *see also* FED. R. CIV. P. 23(g)(2)(D) (in appointing class counsel, court "may include in the appointing order provisions about the award of attorneys' fees"). Moreover, judicial authority to revise agreements on fee allocation has also been recognized in the Rule 23 context; the Agent Orange case is a leading illustration. *See In re* Agent Orange Prod. Liab. Litig., 818 F.2d 216, 218, 226 (2d Cir. 1987), *rev'g* 611 F. Supp. 1452 (E.D.N.Y. 1985) (reversing post hoc approval of undisclosed fee-sharing agreement among plaintiffs' steering committee that would have provided certain committee members a 300% return on their investment in the form of advances to pay litigation ex-

* How would the use of these tools influence which forms of financing are favored in the first place? How would such interventions affect the costs and availability of financing?[40]

3. *Comparison to Familiar Forms of Funding*

* How does the financing and control structure compare with subrogation to insurers, as is common on the defense side?

* How does the funder's stake compare with familiar forms of partial or total claim transfer, such as in patent or in bankruptcy?

* How does the funder's stake compare with the de facto partial claim transfer achieved by the typical contingency fee?[41]

* How does the financing structure compare with co-counsel arrangements in which one law firm helps fund the litigation but exercises only minimal control?[42]

* How does the financing structure differ from these more common analogues, in the existence or absence of fiduciary duties? Or in other ethical constraints? How do they differ in the degree of control (formal or informal) over the conduct of litigation?

* How might existing judicial tools and policies concerning these more familiar forms of litigation financing — subrogation, claim transfers, contingency fees, and co-counsel financing — also be applied or adapted to the newer forms of third-party financing?

---

penses); *see also In re* FPI/Agretech Sec. Litig., 105 F.3d 469, 473–76 (9th Cir. 1997) (permitting district court to disturb fee allocation agreement among class co-counsel); Smiley v. Sincoff, 958 F.2d 498, 501 (2d Cir. 1992) (noting district courts' broad discretion to "establish fee structures," "determine . . . the method of computation of fees," and "modify tentative fee agreements between the parties themselves, even if such agreements were arm's length transactions").

40. I thank Jack Coffee for useful conversations about the potential effects on ex ante pricing of the financing.

41. *See* Garber, *supra* note 2, at 18–19 ("[C]ontingency-fee lawyers have an inherent conflict of financial interest with their clients even without [alternative litigation financing] . . . . The more appropriate question, then, is whether [it] would *exacerbate* (rather than create) such conflicts of interest."); *see also* Molot, *supra* note 2, at 90–92 (discussing attorney contingency fees as "[t]he principal market for litigation claims" in the United States).

42. Such an arrangement was successfully challenged in the Agent Orange litigation. See *supra* notes 14, 39.

C. CAN JUDGES *HARNESS* LITIGATION FINANCE?

Finally, we should remember that there might actually be an upside to the rise of new forms of financing. They may offer new solutions even to very old problems — offering further ways, for instance, for judges to ensure that class members are protected as Rule 23 requires.

First, as Professor Coffee has noted, the right type of litigation financing could serve as an extra check on the system (for instance, with the funder serving as a counterweight to class counsel), just as the large institutional investors serving as lead plaintiff are expected to do in securities litigation under the Private Securities Litigation Reform Act. This would be a system in which "agents are watching agents."[43]

Other possibilities are also imaginable: for instance, litigation financing might supply a party with the funds it needs to hire its preferred counsel, such as one that does not operate on contingency fees.[44] Or, a litigation financing agreement requiring the assent of each plaintiff might in effect convert an opt-out class into an opt-in class, and thus one that is likely to be better informed and possibly more involved in the class action's governance.[45]

I conclude, then, by turning our inquiry toward this possibility — that the courts might seek not only to deflect some possible

---

43. Coffee, *supra* note 2, at 342 & n.173 ("A structure in which the class has both a class counsel and a separate litigation funder is inherently one in which 'agents are watching agents.'" (citing Bernard S. Black, *Agents Watching Agents: The Promise of Institutional Investor Voice*, 39 UCLA L. REV. 811, 817–18 (1992))). For an analysis of how such monitoring and shifting of ownership might work in non-class, mass litigation settings, see Elizabeth Chamblee Burch, *Financiers as Monitors in Aggregate Litigation* 6, (UGA Legal Studies Research Paper No. 1968961), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1968961 (analysis "focus[ing] on the unique dynamics of funding mass litigation that proceeds outside of a class action and explain[ing] how uniting aggregate litigation with third-party financing can reduce agency costs"). *Cf.* David Dana & Max Schanzenbach, *How Would Third Party Financing Change the Face of American Tort Litigation? The Role of Agency Costs in the Attorney-Client Relationship*, NW. L. SEARLE CTR. ON L., REG., & ECON. GROWTH (Sept. 14 2009), http://www.law.northwestern.edu/searlecenter/papers/Schanzenbach_Agency%20Costs.pdf.

44. *See supra* note 25 and accompanying text.

45. *See* Hensler, *supra* note 2, at 321 ("Third-party funding in Australia has had the practical effect of converting an opt-out class action procedure to an opt-in procedure because financing firms require each class member to contract with them."); Picker, *supra* note 25 (elaborating on the argument).

effects of litigation financing, but also to harness others. Could the careful design of financing structures be used to improve representation for class members? Which arrangements will tend to create better monitoring or improve transparency? What might a court, the judiciary, or rule-makers do to promote these beneficial designs?