FINANCIERS AS MONITORS IN AGGREGATE LITIGATION

(forthcoming, New York University Law Review)
Draft date: April 9, 2012

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This Article identifies a market-based solution for monitoring large-scale litigation that proceeds outside of Rule 23's safeguards. Although class actions dominate the scholarly discussion of mass litigation, the ever-increasing restrictions on certifying a class mean that plaintiffs' lawyers routinely rely on aggregate litigation (through multidistrict litigation and liberal joinder devices like Rules 20 and 42) to seek redress for group-wide harms. Despite sharing key features with its class-action counterpart, like attenuated attorney-client relationships, attorney-client conflicts of interest, and high agency costs, no monitor exists in aggregate litigation. Informal group litigation not only lacks Rule 23's judicial protections against attorney over-reaching and self-dealing, but the plaintiffs themselves cannot adequately supervise their attorneys' behavior. A lawyer may represent hundreds or thousands of geographically dispersed plaintiffs, which fosters collective-action problems and makes individual, case-specific information hard to obtain.

The answer to this monitoring problem lies in an unlikely and potentially controversial source: alternative litigation financing. Self-dealing and high agency costs arise principally because of the contingent-fee attorney's dual roles as agent and investor. These roles can pull lawyers in divergent directions; because attorneys front massive litigation costs, they may be tempted to coerce clients into settling so that they can recoup and profit from their investment. Third-party litigation financing can ameliorate this critical conflict by allowing the financier to bear that financial risk. Shorn of financial self-interest, the lawyer is then free to act as a faithful agent. But alternative litigation financing, which involves hedge funds, private investors, and venture capitalists investing in and profiting from large-scale litigation, raises problems of its own and has already sparked a chorus of criticism. Although wedding profit-seeking capitalists and aggregate litigation is certain to spark fireworks, this Article seeks to engineer their union in a way that benefits society as a whole and plaintiffs in particular.

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INTRODUCTION

The class action isn't quite dead, though efforts aimed at extinguishing it have metastasized over the past fifteen years and culminated most recently in the Supreme Court's *Wal-Mart Stores, Inc. v. Dukes* opinion.[1] Without class certification, aggregate

[1] 131 S.Ct. 2541 (2011); Elizabeth Chamblee Burch, *The New Dawn of Nonclass Aggregation*, http://www.scotusblog.com/2011/09/the-new-dawn-of-nonclass-aggregation/ (last visited April 6, 2012) ("Consider, for example, the changes wrought over the past fifteen years by the Private Securities Litigation Reform Act, the Securities Litigation Uniform Standards Act, *Amchem Products, Inc. v. Windsor*, *Ortiz v. Fibreboard Corp.*, and the Class Action Fairness Act, to name but a few.").

litigation offers all of the perils and few of the promises of a class action. Granted, class actions posed problems too,[2] but without the closure they generate and the judge ensuring a fair settlement, lawyers have dreamed up new means for achieving finality that evoke class-action nostalgia. To name but a few, they have exploited the attorney-client relationship to coerce clients into accepting a settlement, threatened to withdraw from representing nonconsenting clients, paid off holdouts to fulfill defendants' demands for complete resolution, forged ongoing "sweetheart" business relationships with settling defendants, and overcompensated weak but prevalent claims to attract more clients.[3]

The problem, in part, is that plaintiffs' attorneys are both financiers and agents and those dual roles sometimes pull them in divergent directions. Just as they did in class actions, lawyers front the costs of litigating massive nonclass cases. But these cases are even more expensive than class actions; attorneys must spend time advertising and recruiting clients. Then they must track each case, hire paralegals to handle the added paperwork, establish specific causation, and spend time persuading each client to settle. Add to that the cost of expert witnesses, investigation, document review, and coordinating with other multidistrict litigation attorneys and the expenses could easily bankrupt a small firm.[4] So, when a defendant puts money on the table—even money with many strings attached, like withdrawing the settlement offer if too few plaintiffs accept it—it tempts plaintiffs' attorneys to strong arm their clients to settle so they can recoup and profit from their financial investment. Because the plaintiff's and the lawyer's interests never overlap perfectly, the lawyer's monetary self-interest and duty of loyalty may be at odds with one another.[5] Yet, nonclass aggregation lacks a monitor to police these settlements the way a judge polices class actions.

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[2] Agency problems in class actions have been frequently discussed. *E.g.*, John C. Coffee, Jr., *The Regulation of Entrepreneurial Litigation: Balancing Fairness and Efficiency in the Large Class Action*, 54 U. CHI. L. REV. 877, 882-83 (1987); 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, 7-8 (1991).

[3] *See e.g.,* Johnson v. Nextel, 660 F.3d 131, 139-40 (2d Cir. 2011) (describing an informal settlement guaranteeing plaintiffs' counsel $2 million to work directly for the defendant as a consultant); *see also* Howard M. Erichson & Benjamin C. Zipursky, *Consent versus Closure*, 96 CORNELL L. REV. 265, 267-68 (2011) (describing how the Vioxx settlement required participating lawyers to withdraw from clients who refused the settlement agreement); Bruce Hay & David Rosenberg, *"Sweetheart" and "Blackmail" Settlements in Class Actions: Reality and Remedy*, 75 NOTRE DAME L. REV. 1377, 1390 (2000) (describing sweetheart settlements); *infra* Part I.B.

[4] "Multidistrict litigation" is a term used for cases that are brought individually, but transferred to a single judge for pretrial handling under the multidistrict litigation statute, 28 U.S.C. § 1407. Though technically for pretrial purposes only, these cases rarely return to their original districts. *See* DeLaventura v. Columbia Acorn Trust, 417 F. Supp. 2d 147 (D. Mass. 2006).

[5] Geoffrey P. Miller, *Some Agency Problems in Settlement*, 16 J. LEGAL STUD. 189, 190 (1987).

Although some judges have likened large multidistrict litigations to class actions and tried to oversee them accordingly,[6] the existence of a legal basis for policing a "voluntary" settlement between private parties is uncertain at best. The clients themselves are unlikely to monitor their attorneys because the very aggregation that increases the economic viability of their claims fosters collective-action problems and makes meaningful information from their attorney difficult to attain.[7] When cases are interdependent, learning the progress of one's own case may yield little information about the overall litigation and vice versa. Plus, individual plaintiffs tend to be unsophisticated about legal matters and trust their attorney's advice—that is, after all, why they hired her.[8]

But the potential for a private monitor does exist in the unlikely guise of third-party financiers—hedge funds, private investors, and venture capitalists. Alternative litigation financing has gradually made its way from Australia and the United Kingdom into the United States, causing substantial controversy in the process. For example, the New York Times has run a critical series of articles titled *Betting on Justice*,[9] the American Bar Association has convened a Commission on Ethics 20/20 Working Group on Alternative Litigation Financing,[10] and the United States Chamber of Commerce recently issued a report entitled *Selling Lawsuits, Buying Trouble*.[11]

Despite the controversy, allowing third parties to fund nonclass aggregation helps to manage principal-agent problems by freeing attorneys from their financial self-interest and encouraging them to act as more faithful agents. It does so by unbundling the attorney's competing roles as investor and advisor, shifting financial

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[6] *See infra* notes 66-70 and accompanying text.

[7] JACK B. WEINSTEIN, INDIVIDUAL JUSTICE IN MASS TORT LITIGATION 11-12 (1995); Deborah R. Hensler, *As Time Goes By: Asbestos Litigation After* Amchem *and* Ortiz, 80 TEX. L. REV. 1899, 1913 (2002); Charles Silver, *Ethics and Innovation*, 79 GEO. WASH. L. REV. 754, 756 (2011).

[8] Robert W. Gordon, *The Independence of Lawyers*, 68 B.U. L. REV. 1, 30 (1988); Samuel Issacharoff & Daniel R. Ortiz, *Governing through Intermediaries*, 85 VA. L. REV. 1627, 1639 ((1999); Russell Korobkin & Chris Gutherie, *Psychology, Economics, and Settlement: A New Look at the Role of the Lawyer*, 76 TEX. L. REV. 77, 82 (1997).

[9] Binyamin Appelbaum, *Betting on Justice; Putting Money on Lawsuits, Investors Share in the Payouts*, N.Y. TIMES, Nov. 15, 2010, at A1 [hereinafter Appelbaum, *Betting on Justice*]; Binyamin Appelbaum, *Taking Sides in a Divorce, Chasing Profit*, N.Y. TIMES, Dec. 5, 2010, at A1; Binyamin Appelbaum, *Lawsuit Loans Add New Risk for the Injured*, N.Y. TIMES, Jan. 17, 2011, at A1; Binyamin Appelbaum, *Lobby Battle Over Loans for Lawsuits*, N.Y. TIMES, Mar. 10, 2011, at B1; *see also* Ashby Jones, *The Next National Investment Craze: Lawsuits!*, WALL ST. J. L. BLOG (June 4, 2010, 12:36 PM), http://blogs.wsj.com/law/2010/06/04/the-next-national-investment-craze-lawsuits/.

[10] *See* ABA COMM'N ON ETHICS 20/20, CALL FOR COMMENT: ISSUES PAPER CONCERNING LAWYER'S INVOLVEMENT IN ALTERNATIVE LITIGATION FINANCING (2010), http://www.americanbar.org/content/dam/aba/migrated/ethics2020/alfposting.authcheckdam.pdf.

[11] U.S. CHAMBER INST. FOR LEGAL REFORM, SELLING LAWSUITS, BUYING TROUBLE: THIRD-PARTY LITIGATION FUNDING IN THE UNITED STATES (2009).

risk to a third party who pays the attorneys on a billable-hour basis (plus, perhaps some small percentage of the recovery as a bonus), and putting in place a sizeable stakeholder with the sophistication and incentive to monitor the agents. If plaintiffs assign a financier a portion of the litigation's proceeds (as the contingent fee does now) in exchange for financing the lawsuit on a nonrecourse basis, the financier would become a super stakeholder.

Incentivizing a super stakeholder to monitor the attorneys was, after all, the basic premise behind Elliott Weiss and John Beckerman's article, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*,[12] which suggested that sophisticated, institutional investors with the most at stake—and thus the most incentive to monitor class attorneys—should serve as lead plaintiffs in securities class actions. Like institutional investors, financiers possess the legal acumen and financial impetus to act as intermediaries by negotiating better hourly rates and requiring attorneys to keep their travel budgets reasonable. But unlike Weiss and Beckerman's proposal, paying attorneys on a billable-hour basis also changes their motivations such that if a financier pushed for a quick settlement, an attorney's self-interest would counterbalance the financier's. The billable hour encourages the lawyer to prolong litigation and spend time advising her clients about the risks of litigating versus settling. Plus, it alleviates the financial worries that prompted attorneys to pressure their clients to settle.

Third-party financiers have already started funding aggregate litigation: Napoli Bern made headlines when it borrowed some $35 million from Counsel Financial to fund the ground zero workers' personal-injury cases against the City of New York and tried to pass $6.1 million in interest costs onto the workers.[13] Burford Capital is funding thousands of Ecuadorian plaintiffs in their controversial personal-injury battle against Chevron.[14] Likewise, in a toxic-tort case against BNSF Railway, attorney Jared Woodfill borrowed more than $3.5 million from a hedge fund to help finance litigation on behalf of some 400 plaintiffs with skin and gastrointestinal

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[12] Elliott J. Weiss & John S. Beckerman, *Let the Money Do the Monitoring: How Institutional Investors Can Reduce Agency Costs in Securities Class Actions*, 104 YALE L.J. 2053, 2109 (1995). Their work lead Congress to enact the PSLRA. S. REP. NO. 104-98, at 11 n.32 (1995), *reprinted in* 1995 U.S.C.C.A.N. 679, 690.

[13] Appelbaum, *Betting on Justice*, *supra* note 9; Joseph Goldstein & Susan Edelman, *Ill Heroes Must 'Shel' Out; Silver Firm Gets Cut of 9/11-Suit Payouts*, N.Y. POST, Aug. 22, 2010.

[14] Lawrence Hurley, *'Master of Disaster' Dons New Guise as Plaintiffs' Attorney in Pollution Case*, N.Y. TIMES, Feb. 1, 2011, http://www.nytimes.com/gwire/2011/02/01/01greenwire-master-of-disaster-dons-new-guise-as-plaintiff-74496.html?pagewanted=all; Roger Parloff, *Have You Got a Piece of This Lawsuit?*, FORBES, June 28, 2011. There is, perhaps an ironic link between the two cases: James Tyrrell, the plaintiffs' lawyer in the case against Chevron, defended New York City and 150 contractors against the ground zero workers claims.

cancers allegedly caused by chemicals used to make railroad ties.[15] These financing arrangements, however, do not follow this Article's blueprint. Lending money to plaintiffs' law firms on a *recourse* basis (where the firm must repay the loan regardless of whether it wins or loses the lawsuit), as was the case for Napoli Bern and Jared Woodfill, may either intensify the pressure on plaintiffs to settle or present them with unexpected interest charges. As this suggests, the way in which financiers bankroll aggregate litigation is critical; this new relationship raises a panoply of questions about maintenance, champerty, barratry, confidentiality, privileges, consent, decisionmaking authority, and incentives. And while scholars such as Richard Epstein, Keith Hylton, Jonathan Molot, Anthony Sebok, and Paul Rubin have written about the economic and professional responsibility implications of third-party financing,[16] neither economists, ethicists, nor complex-litigation scholars have considered financing as a means for addressing the distorted lawyer-client relationship in mass litigation.

This Article focuses on the unique dynamics of funding mass litigation that proceeds outside of a class action and explains how uniting aggregate litigation with third-party financing can reduce agency costs.[17] Part I first highlights the growing prevalence of nonclass aggregation, identifies how it affects plaintiffs' attorneys' risks and financial calculations, and notes its potential impact on substantive enforcement goals. Second, this Part chronicles the ways in which attorneys may act contrary to their principals' interests through shirking or self-dealing. The circumstances of mass litigation exacerbate these unethical tendencies: defendants continue to demand finality in exchange for settling, but plaintiffs' counsel's efforts to provide finality and recover their financial investment without class certification drive them to push the limits of professional responsibility. Despite quasi-ethical practices, there is no meaningful supervision of these settlements. Thus, this Part draws the link between

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[15] Appelbaum, *Betting on Justice*, *supra* note 9.

[16] *E.g.,* Richard A. Epstein, *The Costly Freedom to Sue*, N.Y. TIMES, Mar. 3, 2011 (questioning whether litigation financing will pressure defendants to settle on disadvantageous terms because of wealth inequality); Keith N. Hylton, The Economics of Third-Party Financed Litigation 27 (Aug. 2011) (unpublished manuscript) (suggesting the conditions under which third-part financing can enhance and reduce social welfare), *available at* http://www.masonlec.org/wp-content/uploads/2011/07/Hylton-Revised-Draft1.pdf; Jonathan T. Molot, *Litigation Finance: A Market Solution to a Procedural Problem*, 99 GEO. L.J. 65 (2010) (contending that third-party financing may promote accuracy in adjudication and settlement); Paul H. Rubin, *More Money into Bad Suits*, N.Y. TIMES, Nov. 16, 2010 (claiming litigation in the United States is already excessive and that third-party financing will increase the number of lawsuits); Anthony J. Sebok, *The Inauthentic Claim*, 64 VAND. L. REV. 61, 104-05 (2011) (arguing that historical doctrines like assignment an maintenance do not and should not be barriers to developing third-party litigation).

[17] Because class actions include absent class members, they raise special concerns about notice and consent. This article likewise does not address aggregate litigation in bankruptcy proceedings, such as asbestos.

contingent-fee financing, unethical behavior, and the lack of a supervising monitor to pave the way for Part III's unbundling proposal.

Part II shifts gears slightly to provide background on alternative litigation financing. It surveys the rise in third-party funding, demystifies the various funding types (like the difference between consumer legal funding, loaning money to plaintiffs' law firms, and financing business versus business disputes), and unpacks the myriad incentives that animate diverse financiers, plaintiffs, and their attorneys. This sets the stage for Part III, which explores the potential benefits of disentangling the attorney's role as case-financier from her obligations as a loyal advisor and contemplates how to best allocate decisionmaking control and structure the litigation-financing agreement. As evidenced by the ground zero and BNSF Railway litigation, nonconventional lenders can ensure continued access-to-justice for cases that are uneconomical to pursue individually. And, if the transaction is structured properly, they might likewise supply the oversight and attorney monitoring that nonclass aggregation lacks.

Allowing financiers to act as intermediaries requires some amendments to the existing regulatory landscape. Accordingly, Part III also introduces three categories of regulatory changes to accompany this market-based solution, including administrative-regulatory solutions, judicial forms of oversight, and professional ethics constraints. First, administrative-regulatory solutions include extending the attorney-client privilege to cover financiers through the common-interest doctrine, disclosing potential conflicts of interest between financers and attorneys to clients, and substantively barring instruments that impose negative externalities on plaintiffs. Second, judicial oversight entails submitting the financing arrangement to the judge in camera to discourage unconscionable financing terms, excessive fee arrangements, and collusion between financiers and attorneys. Finally, augmenting professional ethics constraints involves relaxing historical bans on champerty, clarifying conflict-of-interest requirements for attorneys that seek out third-party financing, and loosening confidentiality protections to allow financiers to receive case-specific information.

As these changes suggest, third-party financing can introduce risks, too. These intermediaries add a new wrinkle that cures some of the principal-agent problems, but introduces others. Although financiers will have an incentive to monitor the attorneys, their incentives may not perfectly align with plaintiffs' interests. For instance, litigation that promotes social change by requesting injunctive and declaratory relief, as often occurs in Title VII and civil-rights cases, may well be unattractive to investors who seek to maximize their return. Part IV considers these challenges and weighs these trade-offs, but concludes that introducing third-party financing to aggregate litigation has the potential to improve the status quo.

I. THE PREVALENCE AND COSTS OF AGGREGATE LITIGATION

Over the last fifteen years, the class-action landscape has shifted steadily. Since the mid-1990s, both Congress and the courts have curtailed class actions by providing federal courts with jurisdiction,[18] requiring plaintiffs to prove Rule 23's prerequisites by a preponderance of the evidence,[19] and making class certification more rigorous through a willingness to delve into the merits when they overlap with the certification requirements.[20] Most recently, *Wal-Mart Stores, Inc. v. Dukes* strengthened the commonality standard under Rule 23(a) and ensured that defendants could raise individual defenses, which could inject individual issues into a class that might otherwise meet Rule 23(b)(3)'s predominance requirement.[21] These changes have made certifying a class increasingly difficult, which means that an ever-increasing number of would-be classes proceed en masse through multidistrict litigation and liberal joinder devices, such as Rules 20 and 42.[22]

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[18] The Class Action Fairness Act (CAFA), initially introduced in 1998 and in some form every year thereafter until it passed in 2005. Class Action Fairness Act of 2005 § 2(a), (b), Pub. L. No. 109-2, 119 Stat. 4, 5 (codified in scattered sections of 28 U.S.C.); Class Action Fairness Act of 2004, S. 2062, 108th Cong. (2004); Class Action Fairness Act of 2003, S. 274, 108th Cong. (2003); Class Action Fairness Act of 2002, H.R. 2341, 107th Cong. (2002); Class Action Fairness Act of 2001, S. 1712, 107th Cong. (2001); Class Action Fairness Act of 2000, S. 353, 106th Cong. (2000); Interstate Class Action Jurisdiction Act of 1999, H.R. 1875, 106th Cong. (1999); Class Action Fairness Act of 1999, S. 353, 106th Cong. (1999); Class Action Fairness Act of 1998, S. 2083, 105th Cong. (1998).

[19] *See, e.g.*, *In re* Hydrogen Peroxide Antitrust Litig., 552 F.3d 305, 307 (3d Cir. 2008); Oscar Private Equity Invs. v. Allegiance Telecom, Inc., 487 F.3d 261 (5th Cir. 2007); *In re* IPO Sec. Litig., 471 F.3d 24, 41 (2d Cir. 2006); Szabo v. Bridgeport Machs., Inc., 249 F.3d 672, 676 (7th Cir. 2001).

[20] *See, e.g.*, *Hydrogen Peroxide Antitrust Litig.*, 552 F.3d at 307; *Oscar*, 487 F.3d at 261; *IPO Sec. Litig.*, 471 F.3d at 41; *Szabo*, 249 F.3d at 676; *see also* PRINCIPLES OF THE LAW OF AGGREGATE LITIGATION § 2.06 (2011).

[21] 131 S. Ct. 2541, 2559-61 (2011) (As Justice Scalia explained, under Title VII, "if the employer can show that it took an adverse employment action against an employee for any reason other than discrimination"—showing up late, poor customer service, false information on an application, or insubordination—"the court cannot order the 'hiring, reinstatement, or promotion of an individual as an employee, or the payment to him of any backpay."). For previous cases noting that class certification could be proper despite the availability of individual affirmative defenses, see, Smilow v. Southwestern Bell Mobile Sys., Inc., 323 F.3d 32, 39-40 (1st Cir. 2003); Aliotta v. Gruenberg, 237 F.R.D. 4, 12 (D. D.C. 2006); Dupler v. Costco Wholesale Corp., 249 F.R.D. 29, 46 (E.D.N.Y. 2008). As for commonality, what matters now is not whether plaintiffs can raise common questions, but whether "a classwide proceeding [can] generate common answers apt to drive the resolution of the litigation." *Id.* at 2559 (quoting Richard A. Nagareda, *Class Certification in the Age of Aggregate Proof*, 84 N.Y.U. L. REV. 97, 132 (2009)).

[22] FED. R. CIV. P. 20, 42; *see also* Emery G. Lee III & Thomas E. Willging, *Impact of the Class Action Fairness Act on the Federal Courts: Preliminary Findings from Phase Two's Pre-CAFA Sample of Diversity Class Actions*, 256 F.R.D. 214, 219 tbl. 4 (2009) (showing a decline in class certification motions from 70 percent of cases in 1996 to just twenty-four percent in 2009); Thomas E. Willging & Emery G. Lee III, *From Class Actions to Multidistrict Consolidations: Aggregate Mass-Tort Litigation After* Ortiz, 58 U. KAN.

This shift away from class actions leads to two concerns. First, because large class actions yielded substantial plaintiffs' attorneys' fees,[23] smaller classes and nonclass aggregation may be more expensive—and thus less attractive—business ventures. Funding an all-inclusive class action, particularly a Rule 23(b)(2) class where members cannot opt out, is far more economical for plaintiffs' attorneys than filing thousands of individual claims. This means that fewer attorneys may enter the field, which could dampen competition among the plaintiffs' bar and eventually affect the quality of the representation and the ability to sue.[24] Moreover, because aggregate lawsuits are more expensive for plaintiffs' attorneys to initiate (due principally to client advertising and administrative costs), this may trigger an access-to-justice problem, undermine private enforcement efforts, and cause a market gap in litigation funding.

As this section discusses, in the short term, these added expenses most likely mean that existing plaintiffs' firms with insufficient capital will look increasingly to third-party funders such as hedge funds and private investors to cover litigation costs. Alternative funding sources have proven controversial even in run-of-the-mill litigation, such as car accidents and other personal-injury cases. Not surprisingly, aggregate litigation compounds the controversy.

Second, as more cases proceed as nonclass aggregation, attorneys will continue to experiment with ethically questionable means for achieving litigation closure and recouping their financial investment. In mass torts, without the closure that class settlements once delivered, attorneys on both sides of the aisle have turned to private contracts to achieve finality. Settlements regularly include walk-away provisions that allow defendants to withdraw their offer if too few claimants agree, and some require participating plaintiffs' attorneys to recommend the deal to 100 percent of their clients and to withdraw from representing those who decline.[25] Others add "bonus"

L. REV. 775, 793 (2010). ("In sum, the existing empirical evidence is consistent with the thesis that class certification has become less likely in the post-*Ortiz* period."). For more information on the differences between class actions and aggregate litigation, see Elizabeth Chamblee Burch, *Procedural Justice in Nonclass Aggregation*, 44 WAKE FOREST L. REV. 1 (2009) (describing the procedural justice problems that arise when aggregate litigation proceeds outside of the class action's protections).

[23] Theodore Eisenberg & Geoffrey P. Miller, *Attorney Fees and Expenses in Class Action Settlements: 1993-2008*, 7 J. EMPIRICAL LEGAL STUD. 248, 250 (2010).

[24] *See* RAND CTR. FOR LAW & PUB. POLICY, THIRD-PARTY LITIGATION FUNDING & CLAIM TRANSFER 18 (2010), http://www.rand.org/pubs/conf_proceedings/2010/RAND_CF272.pdf ("Third-party funding has the potential to make some smaller firms contenders for large cases, which may, in turn, cause increased competition with larger firms.").

[25] Initial Settlement Agreement, *In re* Vioxx Prod. Liab. Litig., No. MDL 01657 para. 1.2.8.1 (E.D. La. 2007), *available at* http://www.merck.com/newsroom/vioxx/pdf/Settlement_Agreement.pdf. After some plaintiffs' attorneys contended the settlement conflicted with ethical rules, it was reinterpreted to mean that the attorneys should recommend the deal only if it was in the client's best interest. Alex Berenson, *Some*

payments if 100 percent of the plaintiffs settle, thereby encouraging social pressure to achieve consensus.[26] Consequently, the second part of this section chronicles these issues and the contingent-fee expenditures that fuel them.

A. Funding Gaps and Fee Awards

Private attorneys are the principal vehicle for enforcing substantive rights in many areas like employment discrimination, securities fraud, products liability, consumer fraud, antitrust, and civil rights.[27] They provide a failsafe for agency capture and a check on government abuse and political overreaching.[28] As the courts and Congress have steadily curtailed the plaintiffs' bar's ability to pursue these cases as class actions, they have affected the means of enforcing a wide range of civil-rights, complex statutory schemes, and constitutional rights that past courts willingly certified as Rule 23(b)(2) class actions.[29] For example, district and appellate courts have already relied on the reasoning in *Wal-Mart Stores, Inc. v. Dukes* to decertify or

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Lawyers Seek Changes in Vioxx Settlement, N.Y. TIMES, Dec. 20, 2007, http://www.nytimes.com/2007/12/20/business/20cnd-vioxx.html. For an overview of how these provisions exert ethical pressure on plaintiffs' counsel, see Howard M. Erichson, *The Trouble with All-or-Nothing Settlements*, 58 U. KAN. L. REV. 979 (2010).

[26] Mireya Navarro, *Ground Zero Workers Reach Deal Over Claims*, N.Y. TIMES, Mar. 12, 2010, at A1.

[27] While the occasional bad-faith lawsuit may still exist, there are substantial barriers to initiating meritless litigation such as the hefty costs of initiating and pursuing large-scale litigation, exacting pleading standards, and Rule 11. Accordingly, I proceed from the notion that most aggregate litigation begins on a good-faith basis. *See generally* Elizabeth Chamblee Burch, *Securities Class Actions as Pragmatic Ex Post Regulation*, 43 GA. L. REV. 63 (2008) (contending that securities class actions play a beneficial role); Elizabeth Chamblee Burch, *CAFA's Impact on Litigation as a Public Good*, 29 CARDOZO L. REV. 2517, 2520-23 (2008) (claiming that class actions can be a public good) [hereinafter Burch, *CAFA's Impact*].

[28] John C. Coffee, Jr., *Litigation Governance: Taking Accountability Seriously*, 110 COLUM. L. REV. 288, 345 (2010).

[29] Plaintiffs previously used Rule 23(b)(2) to litigate race and sex discrimination, Fair Debt Collection Practices Act violations, housing desegregation or discrimination suits, improper police practices, and to enforce the American with Disabilities Act. *E.g.*, Davis v. Coca-Cola Bottling Co. Consol., 516 F.3d 955 (11th Cir. 2008); Bolton v. Murray Envelope Corp., 553 F.2d 881 (5th Cir. 1977); Woodard v. Online Info. Servs., 191 F.R.D. 502 (E.D.N.C. 2000); Irwin v. Mascott, 96 F. Supp. 2d 968 (N.D. Cal. 1999).

decline to certify toxic-tort cases,[30] environmental-law cases,[31] products-liability cases,[32] breach-of-contract claims,[33] and Truth in Lending Act claims.[34]

Although it is difficult to predict exactly how these changes will affect substantive enforcement goals, if the history of mass torts is indicative, it illustrates the adaptability and flexibility of the plaintiffs' bar.[35] Rather than evaporating with the mass-tort class action, plaintiffs' attorneys have moved into nonclass aggregation: 1,832 different law firms participated in products-liability multidistrict litigations from 2004 to 2008 and 1,100 law firms were involved solely in the Vioxx litigation, a case in which roughly 49,000 claimants sued Merck for failing to warn consumers of the risks of heart attack and stroke associated with taking the painkiller.[36] While this suggests that enforcement options remain for individually marketable claims, this transformation puts additional pressure on the agency relationship by adding expense and circumventing well-traveled paths for achieving wholesale resolution. That pressure continues to bedevil mass-tort litigation, and with the tightening of class remedies across-the-board, is likely to spread to group-based litigation in other substantive areas as well.

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[30] *E.g.*, Opinion and Order of the Court Denying Class Certification, Henry v. Dow Chem. Co., No. 03-47775-NZ, slip op. at 2-5 (Mich. Cir. Ct. July 18, 2011), *available at* http://amlawdaily.typepad.com/07202011dow.pdf.

[31] *See, e.g.*, Gates v. Rohm & Haas Co., 2011 WL 3715817, at *4-5 (3d Cir. Aug. 25, 2011) (upholding the district court's refusal to certify CERCLA claims because plaintiffs could not establish commonality).

[32] *See, e.g.*, *In re* Bisphenol-A (BPA) Polycarbonate Plastic Prods. Liab. Litig., 2011 WL 2634248, at *7 (W.D. Mo. July 5, 2011) (refusing to certify a class because individualized damage inquiries and plaintiffs' differing knowledge about the BPA controversy undermined commonality).

[33] *See, e.g.*, Altier v. Worley Catastrophe Response, LLC, 2011 WL 3205229 (E.D. La. July 26, 2011) (declining to certify claims adjusters' breach-of-employment agreement claims because they failed to establish adequate representation and the allegations would require individualized damage determinations).

[34] *See, e.g.*, Haynes v. Planet Automall, Inc., 2011 WL 3555613, at *13 (E.D.N.Y. Aug. 12, 2011) (finding that the two disputed questions concerning whether fees and warranties were part of TILA's finance charge could not "be answered uniformly on a class-wide basis").

[35] Still, some of these cases are likely to disappear from the litigation realm entirely, such as those that defendants can avoid through arbitration agreements, like consumer fraud claims and at least some employment disputes. Although public agencies like the SEC, DOJ, and EEOC can avoid the problems with complying with Rule 23, but they may not be able to obtain the full monetary remedies available to private plaintiffs. *See, e.g.,* Jefferson v. Ingersoll Intern. Inc., 195 F.3d 894, 899 (7th Cir. 1999). This Article focuses on the alternative problem of nonclass aggregation.

[36] Affidavit of Joshua D. Wright, Memorandum in Support of Motion for Reconsideration/Revision of Order Capping Contingency Fees and Alternatively for Entry of Judgment at 19, *In re* Vioxx Prods. Liab. Litig., No. MDL 1657 (E.D. La. Dec. 10, 2008).

Entrepreneurial private attorneys typically do not work for free.[37] Instead, they rely on either congressionally approved fee-shifting statutes or contingent fees to compensate them. The contingent fee is the usual method for remunerating plaintiffs' attorneys in areas like mass torts,[38] whereas Congress authorizes fee-shifting statutes in civil-rights litigation, such as Title VII, the Americans with Disabilities Act, and the Age Discrimination in Employment Act.[39]

In class actions, judges typically employ a percentage of the common-fund method for calculating reasonable contingent-fee awards and the lodestar method for prevailing parties under fee-shifting statutes. Empirical studies, however, have consistently shown that the size of the class's recovery is the "overwhelmingly important determinant" regardless of which test courts use.[40] When class actions were commonplace, few plaintiffs ever opted out, which meant that when courts awarded attorneys' fees based on client recovery, plaintiffs' attorneys tended to receive higher awards.[41] Although all mass litigation is expensive, tightening class-certification standards means more risk and less reward for plaintiffs' lawyers. The current economic climate only makes things worse. Law firms are unable to pay their own expenses, much less take on years of litigation without a payday in sight.[42]

1. The Financial Risks of Aggregate Litigation

Consider first the financial risks involved for plaintiffs' attorneys in all large-scale litigation, then the specific challenges that multidistrict litigation adds. To

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[37] Burch, *CAFA's Impact*, *supra* note 27, at 2520-23.

[38] For information on the economics of contingency fees, see Albert H. Choi, *Allocating Settlement Authority under a Contingent-Fee Arrangement*, 23 J. LEGAL STUD. 585 (2003); Rudy Santore & Alan D. Viard, *Legal Fee Restrictions, Moral Hazard, and Attorney Rents*, 44 J. L. & ECON. 549 (2001).

[39] Age Discrimination in Employment Act of 1967, 29 U.S.C. § 626(b) (2006); Civil Rights Attorney's Fees Awards Act of 1976, 42 U.S.C. § 1988(b) (2006); Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e-5(k) (2006); Americans with Disabilities Act of 1990, 42 U.S.C. § 12205 (2006). In "fee-shifting" statutes, courts use the lodestar method to award reasonable fees. *See, e.g.*, Staton v. Boeing Co., 327 F.3d 938, 965 (9th Cir. 2003). Courts employing a lodestar method multiply the reasonable number of attorney hours by a reasonable hourly rate and then use various factors to adjust the final rate. *E.g.,* Gisbrecht v. Barnhart, 535 U.S. 789 (2002); *see also* Charles Silver, *Due Process and the Lodestar Method: You Can't Get There from Here*, 74 TUL. L. REV. 1809 (2000).

[40] Eisenberg & Miller, *supra* note 23, at 250. On fee-shifting statutes generally, see Note, *State Attorney Fee Shifting Statutes: Are We Quietly Repealing the American Rule?*, 47 LAW & CONTEMP. PROBS. 321, 322-23 (1984).

[41] Theodore Eisenberg & Geoffrey P. Miller, *Attorney Fees in Class Action Settlements: An Empirical Study*, 1 J. EMPIRICAL LEGAL STUD. 27, 28-29 (2004) ("We find that the level of client recovery is by far the most important determinant of the attorney fee amount. . . .").

[42] As one law firm's founding partner explained in the process of going out of business, "It's a sign of the current times. Banks are getting a lot more nervous with law firm finance and are pulling loans more quickly." Ben Moshinsky, *Focus: Orchard Solicitors, Til Debt Do Us Part*, THE LAW., Mar. 16, 2009, http://www.thelawyer.com/focus-orchard-solicitors-til-debt-do-us-part/137154.article.

initiate aggregate litigation, attorneys must develop both "generic" and "specific" assets.[43] Generic assets include things like expert witnesses and discovery documents that establish general causation and apply broadly to the attorney's portfolio of similarly situated clients. Just a typical failure-to-warn claim requires understanding how much the medical community knew about the risk before a plaintiff could ever demonstrate that the defendant breached its duty. And this requires experts, document review, witness interviews, and extensive timelines about who knew what and when.[44] These assets are particularly risky to develop given that other lawyers could free ride on one attorney's investment. Specific assets, on the other hand, include the substantial expense of developing the facts of each client's case as well as proving specific causation—that the product caused *this* plaintiff's injury or that an employer discriminated against *this* employee.[45]

Developing these assets takes substantial time and capital. Investments can take years to recoup, which means that plaintiffs' law firms might have to pool their resources, borrow funds from banks, or, as explored in Part III, request financing from third parties.[46] Back in 1995, long before today's recession, attorney Michael Pretl, who sued A.H. Robbins in the Dalkon Shield litigation reported: "We handled over 1,000 Dalkon cases, and it took 20 years before we showed a profit . . . We borrowed heavily at high interest rates to finance the litigation. Even though we settled $55 million in claims, this will be the first year we'll be in the black."[47] Vioxx is a more recent example. One plaintiffs' lawyer estimated that a single Vioxx case initially cost between $1 million and $1.5 million to develop.[48] But once the attorneys turned their collective wisdom into trial packages and put the infrastructure in place, others could litigate similar cases for around $200,000.[49]

Creative financing schemes that help cover and disperse these costs are nothing new. After spending more than $3 million on the Agent Orange litigation in the mid-1980s, plaintiffs' attorneys could not afford to continue litigating.[50] To avoid

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[43] RICHARD A. NAGAREDA, MASS TORTS IN A WORLD OF SETTLEMENT 13-14 (2007).

[44] *Id.* at 13.

[45] *Id.*; Stephen C. Yeazell, Brown*, the Civil Rights Movement, and the Silent Litigation Revolution*, 57 VAND. L. REV. 1975, 1194-95 (2004) ("[I]n lawsuits, law is relatively cheap, but facts are typically expensive.").

[46] NAGAREDA, *supra* note 43, at 14.

[47] Gregory C. Baumann, *Wanted: Law Firm with Guts; State Makes Casting Call for Counsel to Sue on Tobacco's Medicaid Bill*, THE DAILY RECORD, Nov. 17, 1995, at 1.

[48] Joe Nocera, *Forget Fair; It's Litigation as Usual*, N.Y. TIMES, Nov. 17, 2007, http://www.nytimes.com/2007/11/17/business/17nocera.html?pagewanted=all.

[49] *Id.*

[50] JACK B. WEINSTEIN, INDIVIDUAL JUSTICE IN MASS TORT LITIGATION 77 (1995). Agent Orange is a chemical defoliant manufactured by Monsanto, which was used at the government's request during the Vietnam War.

dismissing the case, a reconstituted Plaintiffs' Management Committee allowed six of the nine members to advance funds toward developing generic assets, but each dollar the "investor-attorney" funded would be repaid threefold if plaintiffs' prevailed—a 300 percent return.[51] Judge Weinstein and the Second Circuit reached conflicting outcomes on this arrangement's permissibility.[52] Judge Weinstein insisted that the Committee increase the decisionmaking authority of the lawyers working on the case, as opposed to those just investing in it, but sidestepped the ethical dilemmas by considering the Committee an ad hoc law firm.[53] Because the Committee shared traditional obligations of loyalty and confidentiality to class members and "served only to redistribute attorneys' fees," not to reduce client benefits, the only danger was that "investor" members might clamor to settle early so they could recoup their investment.[54] The Second Circuit, on the other hand, disagreed with the law-firm analogy, found that the agreement created impermissible conflicts of interests between the investor attorneys and the class, and invalidated the agreement.[55]

2. The Added Risks of Multidistrict Litigation

Creative financing schemes like those used in Agent Orange may be the best way to conduct today's litigation given the additional risks inherent in multidistrict litigation. First, plaintiff's lawyers must now take on substantial administrative costs. In nonclass aggregation, attorneys recruit and interact with individual clients, which is significantly more expensive than interacting with a few class representatives and receiving fees based on benefitting the whole class.[56] For instance, attorneys in the Vioxx Litigation Consortium considered 30,000 potential clients and accepted only 2,000, but the process itself took a combined 1,601,150 hours by staff, paralegals, attorneys, nurse practitioners, and medical experts at a cost of $13.5 million.[57]

Second, multidistrict litigation increases coordination costs and decreases attorney control. Although class-action attorneys must often coordinate among large legal teams and sometimes jockey with other attorneys to become class counsel, multidistrict litigation significantly alters these dynamics. Coordination typically

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[51] Vincent Robert Johnson, *Ethical Limitations on Creative Financing of Mass Tort Class Actions*, 54 BROOK. L. REV. 539, 549-50 (1988).

[52] *In re* Agent Orange Prod. Liab Litig., 818 F.2d 216, 221 (2d Cir. 1987); *In re* Agent Orange Prod. Liab. Litig., 611 F. Supp. 1296, 1452 (E.D.N.Y. 1985);

[53] *In re* Agent Orange Prod. Liab. Litig., 611 F. Supp. at 1461; WEINSTEIN, *supra* note 50, at 77.

[54] *In re* Agent Orange Prod. Liab. Litig., 611 F. Supp. at 1460; WEINSTEIN, *supra* note 50, at 77 - 78.

[55] *In re* Agent Orange Prod. Liab. Litig., 818 F.2d at 225-26; Johnson, *supra* note 51, at 553.

[56] Joshua Hamerman, *A PE Fund to Sponsor Corporate Litigation*, INVESTMENT DEALERS' DIG., Jan. 22, 2010, at 1 ("In the U.K. [where class actions are opt-in], you literally recruit claimants one by one, and as a result the administrative costs can become very large relative to the action.").

[57] Charles Silver & Geoffrey P. Miller, *The Quasi-Class Action Method of Managing Multi-District Litigations: Problems and a Proposal*, 63 VAND. L. REV. 107, 128 (2010).

occurs both informally and formally. Informally, plaintiff's attorneys may form groups and coalitions on their own, such as the Vioxx Litigation Consortium (which included lawyers from five law firms) and the Polybutylene Plumbing Litigation (which included forty-nine law firms).[58] Formally, judges handpick experienced attorneys to serve on executive committees, plaintiffs' steering committees, and specialized committees such as negotiating or fee-allocation committees.[59] These formal and informal aspects often meld. For example, plaintiffs' attorneys selected Chris Seeger and Andy Birchfield as the co-lead attorneys for the Vioxx Plaintiffs' Steering Committee over dinner at Antoine's in New Orleans such that it was a foregone conclusion by the time Judge Fallon formally appointed them to the position.[60] This relegates disfavored attorneys to a secondary status, renders them unable to control their cases, and leads to less compensation.[61]

Third, multidistrict litigation means less certain fee awards. In individual contingent-fee cases, clients sign retainer agreements allocating the attorney around 33 percent of the litigation's proceeds.[62] In class actions, judges award attorneys' fees based on the percentage-of-the-common-fund method (often with a lodestar check), which ranges from 11 to 39 percent, with an average of around 20 percent.[63] But backroom jockeying for key positions, judicial creation of and appointment to various litigation committees, ad hoc fee cuts, and the comparative lack of transparency makes multidistrict litigation a riskier venture.[64] Even though clients

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[58] *In re* Polybutylene Plumbing Litig., 23 S.W.3d 428 (Tex. Ct. App. 2000); Silver & Miller, *supra* note 57, at 126.

[59] Dennis E. Curtis & Judith Resnik, *Contingency Fees in Mass Torts: Access, Risk, and the Provision of Legal Services when Layers of Lawyers Work for Individuals and Collectives of Clients*, 47 DEPAUL L. REV. 425, 431, 434 (1998)

[60] SNIGDHA PRAKASH, ALL THE JUSTICE MONEY CAN BUY 13-14 (2011).

[61] Silver & Miller, *supra* note 57, at 118-20.

[62] Herbert M. Kritzer, *The Wages of Risk: The Returns of Contingency Fee Legal Practice*, 47 DEPAUL L. REV. 267, 284-86 (1998).

[63] Eisenberg & Miller, *supra* note 23, at 258 (studying class action awards from 1993-2008 and observing that "[t]he mean fee to recovery ratio was 0.23, or 23 percent of the class award, but this percent varies by recovery size"); Brian T. Fitzpatrick, *An Empirical Study of Class Action Settlements and Their Fee Awards*, 7 J. EMPIRICAL LEGAL STUD. 811, 831 (2010) (averaging the percent of fees and expenses to be twenty percent of the total settlement amount in 2007).

[64]); Judith Resnik, *Aggregation, Settlement, and Dismay*, 80 CORNELL L. REV. 931 (1995) ("Once a litigant's case becomes a part of an MDL, that litigant cannot 'opt out' during the pretrial phase. Further, under the MDL rubric, trial judges may also appoint lead counsel and plaintiff steering committees, transforming these attorneys into lawyers for a group, albeit lawyers with an even less defined set of ethical obligations than the class action lawyer."); Charles Silver, *The Responsibilities of Lead Lawyers and Judges in Multidistrict Litigations*, 79 FORDHAM L. REV. 1985, 1986-89 (2011) (discussing the ways in which steering committees control multidistrict litigation and how plaintiffs have little control of these attorneys).

involved in multidistrict litigation have individually retained their attorneys and have thus agreed to set contingent fees, some judges reduce and reallocate those fees to compensate attorneys performing common-benefit work and to minimize plaintiffs' litigation costs.[65]

In the *Guidant* litigation, for example, Judge Frank's fee cap meant that lawyers on the case's outskirts (whose clients had agreed to a 40 percent contingent fee) received only 28 percent of their client's gross recovery.[66] Uncertainty also plagues the "chosen" lawyers on the inside, as the recent Vioxx skirmish over $350 million in common-benefit fees demonstrated. Divvying up the $350 million required a special committee, a discovery master, rounds of objections, a week-long hearing, and, ultimately, a 132-page order from Judge Fallon.[67]

The same uncertainty principal held true in the ground zero workers case where Judge Hellerstein cut plaintiffs' attorneys fees from the contractual amount of 33 percent to 25 percent and prohibited them from charging clients some $6.1 million in interest costs from third-party financing.[68] Plus, when more than 95 percent of plaintiffs consented to the proposed settlement and thereby swelled their compensation from $625 million to $680 million, Judge Hellerstein forbade their lawyers from sharing in the increase. He explained, "Such fees, taken after plaintiffs' counsel have had all their expenses paid out of the settlement funds, are more than sufficient to compensate counsel for their representation."[69] Plaintiffs' lawyers, on the other hand, struggled with whether to appeal the ruling. One lead attorney explained, "We should be paid because it was part of the deal" and the bonus payments were "something we had to litigate."[70]

Of course, in some ways, hindsight makes it easy to cut fees and contend that plaintiffs' attorneys are overcompensated, particularly when some free ride on others' efforts and benefit from economies of scale. Still, litigation's risks and rewards cannot be measured in a single case; instead, lawyers tend to think of contingent-fee cases as a portfolio of risk.[71] Diversifying cases diversifies risk, which means that the

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[65] Silver & Miller, *supra* note 57, at 139.

[66] *In re* Guidant Corp. Implantable Defibrillators Prods. Liab. Litig., No. MDL 05-1708, 2008 WL 3896006, at *9-10 (D. Minn. Aug. 21, 2008); Silver & Miller, *supra* note 57, at 128-30.

[67] *In re* Vioxx Prods. Liab. Litig., 802 F. Supp. 2d 740 (E.D. La. 2011); Alison Frankel, *Vioxx Judge Steps in to Split $350 ml Plaintiffs Lawyer Pie*, REUTERS, Aug. 11, 2011, http://blogs.reuters.com/alison-frankel/2011/08/11/vioxx-judge-steps-in-to-split-350-ml-plaintiffs-lawyer-pie/.

[68] Mark Hamblett, *Plaintiffs Lawyers in 9/11 Cases Lose Bid to Recoup $6.1 Million in Interest*, N.Y. L.J. Aug. 30, 2010, at 1.

[69] Mireya Navarro, *Terms Met, Payout Rises for Workers at 9/11 Site*, N.Y. TIMES, Sept. 13, 2011, at A28.

[70] *Id.*

[71] HERBERT M. KRITZER, RISKS, REPUTATIONS, AND REWARDS: CONTINGENCY FEE LEGAL PRACTICE IN THE UNITED STATES 10-18 (2004); Jonathan T. Molot, *How U.S. Procedure Skews Tort Law*

winning cases not only finance the costs of those cases, but the costs of the losing cases as well.[72] It is this insurance-like dimension of spreading risk across clients that judges may sometimes fail to appreciate.[73]

Diversification, however, is easier in individual litigation, which is why attorneys who practice in aggregate litigation often turn to creative financing arrangements to spread risk. Historical doctrines like champerty and barratry would ban not only these arrangements, but class actions, too, because they promote "officious intermeddling in a suit that belongs to no one" and "excit[e] and stir[] up suits and quarrels."[74] But concerns about deterring wrongdoing and equitably compensating large plaintiff groups have long trumped these antiquated deontological and professional concerns. Eliminating old bars against contingent-fee arrangements and compensating class counsel based on common-fund and restitutionary theories encourage non-governmental lawyers to act on behalf of plaintiffs who lack the economic incentive or funding to sue.[75] So, while we are no longer concerned about exciting and stirring up mass litigation, using the contingent fee to compensate plaintiffs' attorneys had lead to a new concern: it can distort incentives in the lawyer-client relationship.

B. Aggregation Minus a Monitor: Agency Costs as a Bundling Problem

Contingent fees augment the lawyer-client relationship by making the attorney the financier. She is an agent, a creditor, an investment banker, and a risk manager; the litigation is a joint venture with the client.[76] But bundling these two roles—financier and advisor—is what breeds most attorney-client conflicts of interest. To be sure, other billing arrangements create perverse incentives, too. Hourly billing incentivizes attorneys to work slowly and prolong the lawsuit by filing unnecessary motions, and even pro bono services may encourage attorneys to skimp on research and development so that they can return to paying clients. But contingent fees

Incentives, 73 IND. L. J. 59, 82 (1997); Richard W. Painter, *Litigating on a Contingency: A Monopoly of Champions or a Market for Champerty?*, 71 CHI.-KENT L. REV. 625, 678-80 (1995).

[72] KRITZER, *supra* note 71, at 16.

[73] *Id.*

[74] 4 W. BLACKSTONE, COMMENTARIES ch. x §§ 12-13, 135 (Tucker ed. 1803).

[75] *See* Boeing Co. v. Van Gemert, 444 U.S. 472, 473 (1982); Charles Silver, *A Restitutionary Theory of Attorneys' Fees in Class Actions*, 76 CORNELL L. REV. 656, 663-66 (1991).

[76] *See id.*; John C. Coffee, Jr., *Professional Responsibility and the Corporate Lawyer*, 13 GEO. J. LEGAL ETHICS 331, 340-41 (2000) (observing the same phenomenon in the class-action context); Charles Silver, *Merging Roles: Mass Tort Lawyers as Agents and Trustees*, 31 PEPP. L. REV. 301, 302 (2003) (positing that Coffee's argument applies with equal force to mass-tort representations because "[t]he plaintiffs' attorneys provide crucial financing").

spawn nearly all the quintessential agency problems in aggregate litigation.[77] As Judge Weinstein observed after handling the Agent Orange, asbestos, and DES cases, most mass-tort lawyers have been "focused on getting cash for the individual client, obtaining a large fee, and closing the file as quickly and with as little effort as possible."[78]

Contingent fees are less problematic in individual and class litigation. In individual litigation, a plaintiff can monitor the attorney herself. Although she may lack the expertise to evaluate legal arguments and motions, she can insist that the attorney explain things to her, request additional information, and determine whether the agent conforms to her expectations. Because class members are typically uninvolved in class actions, we impose fiduciary duties on the attorney to act in the whole class's best interest and require the judge to certify that the attorney adequately represents the class, ensure that any settlement is fair, reasonable, and adequate, and approve attorneys' fee requests.[79] But nonclass aggregation, which typically proceeds as multidistrict litigation, lacks these monitoring options. Clients are disaggregated and a single attorney often represents hundreds or thousands of clients with roughly similar claims, which makes meaningful client monitoring difficult.[80] And because judges do not certify plaintiffs' claims as a class, the judge has far less authority to police the agency relationship or the settlement.

My point is not that all or even most plaintiffs' attorneys are unethical, but that the current incentive structure is open to abuse. Paying attention to situations in which attorneys' interests diverge from their clients' interests and eliminating some sources of tension can foster fidelity and loyalty. Consequently, this section includes theoretical situations in which the attorney's interests might diverge from her client's and illustrative, anecdotal evidence of lawyer misconduct.[81]

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[77] For background on the principal-agent problems with contingency fees, see, e.g., Geoffrey Miller, *Some Agency Problems in Settlement*, 16 J. LEGAL STUD. 189 (1987); James D. Dana, Jr. & Katherine E. Spier, *Expertise and Contingent Fees: The Role of Asymmetric Information in Attorney Compensation*, J. L. ECON. & ORG. 349 (1993); A. Mitchell Polinsky & Daniel Rubinfeld, *Aligning the Interests of Lawyers and Clients*, 5 AM. L. & ECON. REV. 165 (2003).

[78] WEINSTEIN, *supra* note 50, at 47.

[79] FED. R. CIV. P. 23; Reynolds v. Beneficial Nat'l Bank, 288 F.3d 277 (7th Cir. 2002); Chris Brummer, Note, *Sharpening the Sword: Class Certification, Appellate Review, and the Role of the Fiduciary Judge in Class Action Lawsuits*, 104 COLUM. L. REV. 1042, 1060-61 (2004); Nancy Morawetz, *Bargaining, Class Representation and Fairness*, 54 OHIO ST. L.J. 1, 42-46 (1993).

[80] As others and I have suggested, a plaintiffs' steering committee—made up of the claimants, not their attorneys—might also perform a monitoring function. Elizabeth Chamblee Burch, *Litigating Together: Social, Moral, and Legal Obligations*, 91 B. U. L. REV. 87, 126 (2011); Silver, *supra* note 6, at 759. The catch, however, is that for procedural-justice purposes the plaintiffs themselves must still have the opportunity to play a role in group deliberation. Burch, *supra*, at 126.

[81] Of course, these examples may come from outlier cases and not reflect business as usual. The point is to lend context to the analytical observation that the incentive structure is open to abuse, not to suggest that these examples are the norm. There are few empirical studies on disciplinary

1. Quick Settlement Sell-Outs. The tangled advisor-lender relationship may motivate attorneys to cherry-pick stronger cases for trial or settle quickly and cheaply if it means they can collect their contingent fee and move on to other cases.[82] If a defendant offers to settle a case for a nominal value soon after receiving a complaint, the attorney might prefer to accept the offer; she would receive her fee and could then litigate other cases, even if further work might yield a marginally higher value.[83] For example, suppose the attorney thinks that working on the case for another year might produce a settlement offer $300,000 more than whatever the current offer is, but that year of work would cost her $150,000. Assuming a one-third contingent fee, she would receive only $100,000, but the clients might want her to press forward since their settlement value would still be greater. Thus, the attorney's loyalty may divide between her self-interest and her clients' interest.

2. Collusive Settlements. A close cousin of the quick settlement, three features contribute to the potential for collusive settlements: "repeat player" attorneys who routinely represent plaintiffs (one-shotters) or defendants (repeat players or, occasionally, one-shotters); aggregation before a single court; and a judge who wants to clear her docket.[84] Because developing case-specific expertise is costly, both plaintiff and defense attorneys specialize, which means that a relative handful of repeat-player law firms handle the majority of mass-tort or employment-discrimination cases, for instance.[85] Consider the Dalkon Shield litigation: six attorneys represented 8,039 claimants (an average of 1,340 each), and forty-three attorneys represented the remaining 13,174 claimants.[86] Likewise, only a handful of plaintiffs' law firms represented asbestos plaintiffs,[87] and asbestos defense attorneys

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violations that offer hard evidence of these practices and many violations remain unreported. One study that does exist did not specifically examine aggregate litigation or class actions, but demonstrated a high percentage of disciplinary violations among plaintiffs'-side personal injury attorneys. Patricia W. Hatamyr & Kevin M. Simmons, *Are Women More Ethical Lawyers? An Empirical Study*, 31 FLA. ST. U. L. REV. 785, 818 tbl. 12 (2004).

[82] Charles Silver, *Merging Roles: Mass Tort Lawyers as Agents and Trustees*, 31 PEPP. L. REV. 301, 306-07 (2003).

[83] Geoffrey P. Miller, *Some Agency Problems in Settlement*, 16 J. LEGAL STUD. 189, 190 (1987).

[84] *See, e.g.*, St. Louis Sw. Ry. Co. v. Voluntary Purchasing Grps., Inc., 929 S.W.2d 25 (Tex. Ct. App. 1996); *see also* Marc Galanter, *Why the "Haves" Come Out Ahead: Speculations on the Limits of Legal Change*, 9 LAW & SOC'Y REV. 95, 97-103 (1974); Samuel Issacharoff, *Class Action Conflicts*, 30 U.C. DAVIS L. REV. 805, 807 (1997).

[85] John C. Coffee, Jr., *Class Wars: The Dilemma of the Mass Tort Class Action*, 95 COLUM. L. REV. 1343, 1358-59 (1995).

[86] Georgene M. Vairo, *Reinventing Civil Procedure: Will the New Procedural Regime Help Resolve Mass Torts?*, 59 BROOK. L. REV. 1065, 1075 n.47 (1993).

[87] Deborah R. Hensler & Mark A. Peterson, *Understanding Mass Personal Injury Litigation: A Socio-Legal Analysis*, 59 BROOK. L. REV. 961, 966 (1993).

organized a single consortium to negotiate settlement.[88] Because repeat players know that they will meet again, they may adjust their litigation tactics and settlements to reflect past interactions and future negotiations rather than the present case's merits.[89] Class actions contain built-in protections that help guard against this problem: judges must review class settlements for fairness, reasonableness, and adequacy; class objectors can object to unfair terms and attorneys fees; and state attorney's general can intervene and object.[90] Nonclass aggregation, on the other hand, lacks these safeguards.

3. Underfunded Litigation. Because the contingent-fee attorney acts as a financier and aggregate litigation is expensive, a very real danger exists that the attorney may run out of resources with which to prosecute the case. This means that she might cut corners in critical areas like expert witness fees or discovery, quickly settle a few cases to bankroll the rest, or request to dismiss the case.[91] For example, though the plaintiffs' attorneys who initiated the Agent Orange litigation spent millions pursuing the case, they eventually exhausted their capital. A new financial group took over, but the same was not true in the New Jersey tobacco litigation.[92] There, plaintiffs' counsel tried to withdraw, but the court refused.[93] Although courts have this kind of authority in class actions,[94] no counterpart exists in aggregate litigation.

Even when attorneys adequately fund the litigation, their cost-sharing agreements can affect strategy. In the New Jersey Vioxx litigation, Judge Carol Higbee proposed bifurcating four cases by trying general liability and then specific causation; the plaintiffs' lawyers had agreed to split the trial costs four ways.[95] But when attorney Mark Lanier disagreed with the cases' presentation order and balked at Judge Higbee's proposal to try his case as a stand-alone, he explained that he'd "put in more time and money on the Vioxx litigation than any other lawyer in the country—16 weeks in two trials and $4-5 million of his money."[96] "I'll be quite

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[88] Harry H. Wellington, *Asbestos: The Private Management of a Public Problem*, 33 CLEV. ST. L. REV. 375, 387-89 (1984). The group was first known as the Asbestos Claims Facility, however, a smaller group, the Center for Claims Resolution (CCR) replaced it and represented twenty-one corporations that manufactured asbestos. Lawrence Fitzpatrick, *The Center for Claims Resolution*, 53 LAW & CONTEMP. PROBS., Autumn 1990, at 13, 17.

[89] *E.g.*, Amchem Prods., Inc. v. Windsor, 521 U.S. 591 (1997); *see also* KRITZER, *supra* note 71, at 15; Edward H. Cooper, *Aggregation and Settlement of Mass Torts*, 148 U. PA. L. REV. 1943, 1951-52 (2000). For a discussion of related problems in the class action, see Hay & Rosenberg, *supra* note 3, at 1390.

[90] FED. R. CIV. P. 23(e), (h); 28 U.S.C. § 1715 (Supp. V 2005).

[91] *See* WEINSTEIN, *supra* note 50, at 77.

[92] *Id.* at 62.

[93] WEINSTEIN, *supra* note 50, at 62.

[94] FED. R. CIV. P. 23(g).

[95] SNIGDHA PRAKASH, ALL THE JUSTICE MONEY CAN BUY: CORPORATE GREED ON TRIAL 32-33 (2011).

[96] *Id.* at 33.

candid with the Court, I really don't think it is fair at this point for me to go try one single case and have a third one go up on appeal with Merck with another $2 million of my money and another six weeks of my time tied up in it."[97] Thus, litigation financing affects a lawsuit in more ways than one.[98]

4. Astronomical Fees. Attorneys invest in and initiate aggregate litigation to profit from fee awards. This is the private-attorney-general model's aim: to encourage private lawyers to initiate civil actions and thereby further the public interest, whether for selfish or altruistic reasons.[99] But attorneys' fee awards usually mean that counsel's stake far exceeds any one client's recovery, which sometimes tempts lawyers to exploit that dynamic by charging unreasonable fees. To combat this temptation in class actions, Rule 23(h) allows the court to award "reasonable attorney's fees and nontaxable costs."[100] By contrast, in individual cases, clients "negotiate" and consent to contingent-fee percentages in the attorney's retainer agreement. Without class certification, aggregate litigation could fall prey to the dangers of fee exploitation; a few seasoned lawyers press the defendant into settling and the other plaintiffs' attorneys free ride on those efforts without earning their fees. Although a few judges have invoked their inherent equitable authority and analogized to class actions and the common-fund doctrine to reduce fee awards in multidistrict litigation,[101] many don't, and the lack of clear authority and guidance for those that do can lead to other inequities.[102]

5. Cram-Down Settlement Practices. Attorneys have routinely devised creative settlement provisions that deter class members from opting out and coax them to accept a settlement. Class-settlement designers have tried to include: most-favored-nation provisions, which assure those who remain in the settlement that those who

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[97] *Id.*

[98] KRITZER, *supra* note 71, at 15; LAURENCE H. ROSS, SETTLED OUT OF COURT: THE SOCIAL PROCESS OF INSURANCE CLAIMS ADJUSTMENT 82 (1980).

[99] *See generally* Burch, *CAFA's Impact*, *supra* note 27, at, 2524 ("Because class litigation performs . . . semi-public activities, the class action plaintiff's bar has been labeled 'private attorneys general."); John C. Coffee, Jr., *Rescuing the Private Attorney General: Why the Model of the Lawyer as Bounty Hunter is Not Working*, 42 MD. L. REV. 215, 218 (1983); Harry Kalven, Jr. & Maurice Rosenfield, *The Contemporary Function of the Class Suit*, 8 U. CHI. L. REV. 684, 687, 721 (1941).

[100] FED. R. CIV. P. 23(h), advisory comm. notes.

[101] *See, e.g.*, *In re* Guidant Corp. Implantable Defibrillators Prods. Liab. Litig., No. MDL 05-1708, 2008 WL 682174, at *5-19 (D. Minn. Mar. 7, 2008) (capping fee awards at 20 percent, subject to the special master's discretion); *In re* Vioxx Prod. Liab. Litig., 574 F. Supp. 2d 606, 607 (E.D. La. 2008) (awarding 32 percent of the common fund to attorneys); (*In re* Zyprexa Prods. Liab. Litig., 424 F. Supp. 2d 488, 491 (E.D.N.Y. 2006) (capping fees at 35 percent of the client's recovery, subject to the special masters' discretion); Navarro, *supra* note 69, at A28.

[102] *See* Silver & Miller, *supra* note 57, at 109-10 (arguing that judicial ability to reduce fees forces lawyers to be overly deferential, inserts unpredictability, and ultimately advantages defendants).

opt out will not receive a better deal and, if they do, that the class will benefit too; liens on the defendant's assets in favor of the class, which requires those who opt out to wait in line for years behind class members before getting paid; and walk-away provisions, which permit the defendant to withdraw the settlement offer if too few claimants consent or too many class members opt out.[103]

In the class context, at least, a judge must decide whether these provisions are fair, reasonable, and adequate.[104] But aggregate litigation does not only lack these judicial safeguards, settlement designers have weakened the one protection claimants have—the attorney's duty of loyalty. Now defendants contract with plaintiffs' law firms (as opposed to plaintiffs themselves), dub their agreement a "settlement," and require plaintiffs' lawyers to withdraw from representing any client who declines the offer.[105] The agency relationship itself leverages plaintiffs' consent.

The Vioxx settlement combined that loyalty lever with an exit clause for Merck. The settlement offer required each participating plaintiffs' attorney to recommend the deal to 100 percent of her clients and to withdraw from representing those who declined.[106] Unless 85 percent of the claimants consented, Merck could walk away and would compensate neither the plaintiffs' nor their attorneys. Plaintiffs who refused the deal and could find alternative representation would continue to litigate before Judge Fallon, who announced his preference for settlement from the beginning and appeared at a press conference to "endorse" the deal.[107]

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[103] *In re* Inter-Op Hip Prosthesis Liab. Litig., 204 F.R.D. 330, 354 (N.D. Ohio 2001) (upholding as fair and reasonable a Rule 23(b)(3) settlement agreement including a most-favored-nation provision as well as a provision that created a lien on defendants' assets; the parties later removed the lien after the Sixth Circuit expressed doubts about the settlement's legitimacy); Kathryn E. Spier, *The Use of "Most-Favored-Nation" Clauses in Settlement of Litigation*, 34 RAND J. ECON. 78, 80 (2003).

[104] FED. R. CIV. P. 23(e).

[105] After some plaintiffs' attorneys contended that this kind of settlement provision in the Vioxx litigation conflicted with ethical rules, it was reinterpreted to mean that the attorneys should recommend the deal only if it was in the client's best interest. Alex Berenson, *Some Lawyers Seek Changes in Vioxx Settlement*, N.Y. TIMES, Dec. 20, 2007, http://www.nytimes.com/2007/12/20/business/20cnd-vioxx.html. For more information on the settlement, see Howard M. Erichson & Benjamin C. Zipursky, *Consent versus Closure*, 96 CORNELL L. REV. 265, 274-92 (2011).

[106] Initial Settlement Agreement, *In re* Vioxx Prod. Liab. Litig., No. MDL 01657 para. 1.2.8.1 (E.D. La. 2007), *available at* http://www.merck.com/newsroom/vioxx/pdf/Settlement_Agreement.pdf.

[107] *See* Jef Feeley & Leslie Snadowsky, *Merck Vioxx Judge Threatens to End Suit Consolidation*, BLOOMBERG, Jan. 5, 2006, http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aOUXOdXoKAX8&refer=top_world_news; *see also* Mark A. Peterson & Molly Selvin, *Mass Justice: The Limited and Unlimited Power of the Courts*, 54 LAW & CONTEMP. PROBS. 227, 230 (1991) ("Faced with mass tort litigation, judges are not simply neutral arbiters; rather, they have strong personal incentives to speed the judicial process, save costs and labor, and reduce redundancy."); Peter H. Schuck, *The Role of Judges in Settling Complex Cases: The Agent Orange Example*, 53 U. CHI. L. REV. 337, 361-62 (1986).

Similarly, in the ground zero workers' case against New York City, settlement designers tried to cram the settlement down through group cohesion. Attorneys offered a close-knit community of firefighters and police officers $575 million if 95 percent of them accepted, but if 100 percent agreed, that amount increased to $657.5 million.[108] In a move that prompted commentators to question the scope of judicial authority in nonclass aggregation, Judge Hellerstein rejected the proposal, dubbed the compensation inadequate, and questioned the large attorneys' fees.[109] Eventually, attorneys increased the settlement amount to $625 million, so long as 95 percent approved; 95.1 percent did.[110]

6. Misallocation of Settlement Funds. To add to the obvious, once defendants decide to settle, they want to end the litigation by including as many plaintiffs as possible. But they care little about how settlement funds are distributed among the claimants and their lawyers.[111] Settlement agreements requiring nearly unanimous consent pressure plaintiffs' attorneys to push their clients to acquiesce so they can collect their fee. Lump-sum settlements, however, where the defendant offers plaintiffs' counsel a sum of money to settle all of her cases, tempts some clients to demand a higher payout in return for consenting.[112]

Lump-sum settlements create an ultimatum game: if a claimant (or enough claimants) rejects the settlement, then no one, including the attorney, receives anything. But buying off the holdout violates the lawyer's ethical obligations to her remaining clients.[113] The temptation is so great, however, that attorneys may attempt to achieve consensus by hook or by crook, as was the case in the aggregate Kentucky

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[108] Navarro, *supra* note 26, at A1.

[109] Mireya Navarro, *Empathetic Judge in 9/11 Suits Seen by Some as Interfering*, N.Y. TIMES, May 3, 2010, at A17.

[110] Mireya Navarro, *Sept. 11 Workers Agree to Settle Health Lawsuits*, N.Y. TIMES, Nov. 20, 2010, at A1.

[111] The infamous Kentucky Fen-Phen Settlement agreement was one such provision. Gallion v. Ky. Bar Ass'n, 266 S.W.3d 802, 803-04 (Ky. 2008); Erichson, *supra* note 25, at 985.

[112] Kerrie M. Brophy, *Consent Waivers in Non-Class Aggregate Settlements: Respecting Risk Preference in a Transactional Adjudication Model*, 22 GEO. J. LEGAL ETHICS 677, 680 (2009); Howard M. Erichson, *Beyond the Class Action: Lawyer Loyalty and Client Autonomy in Non-Class Collective Representation*, 2003 U. CHI. LEGAL F. 519, 572; Howard M. Erichson, *A Typology of Aggregate Settlements*, 80 NOTRE DAME L. REV. 1769, 1787-89 (2005); Charles Silver & Lynn A. Baker, *Mass Lawsuits and the Aggregate Settlement Rule*, 32 WAKE FOREST L. REV. 733, 767 (1997); *cf.* Paul H. Edelman, Richard A. Nagareda & Charles Silver, *The Allocation Problem in Multiple-Claimant Representations*, 14 SUP. CT. ECON. REV. 95, 99 (2006) (noting that because lawyers must pay referral or forwarding fees for some clients, they have an incentive to misallocate in favor of those without fees attached); Bruce L. Hay, *The Theory of Fee Regulation in Class Action Settlements*, 46 AM. U. L. REV. 1429, 1472 (1997).

[113] Erichson, *supra* note 25, at 1011.

Fen-Phen Settlement.[114] Kentucky lawyers William Gallion, Shirley Cunningham, and Melborne Mills had their staff contact their fen-phen clients to tell each how much she would receive. But, in violation of Model Rule of Professional Conduct 1.8(g), they never told their clients the full settlement amount, how much money others would receive, how their settlement amounts were determined, or that they could refuse the settlement and proceed to trial.[115] They offered their clients less than the total settlement and pocketed the rest—fees well above their contingent-fee arrangement.[116]

Though the practices described sound Grisham-esque,[117] they are all too real. Consider, for example, the recent allegations in *Johnsons v. Nextel Communications, Inc.* where many of the practices just discussed occurred in a single nonclass aggregation.[118] In *Johnsons*, a group of 587 clients retained a law firm to sue Nextel for employment discrimination, but instead of suing, the law firm allegedly entered into a dispute-resolution agreement with Nextel that included kickbacks for the firm.[119] Nextel would pay plaintiffs' firm $2 million to convince its clients to abandon their legal claims and enter into an expedited mediation or arbitration procedure, an additional $3.5 million as clients' claims were resolved, and $2 million to work directly for Nextel—the defendant—as a consultant for two years afterward.[120] Moreover, if the attorneys could not persuade their clients to accept the settlement (and quickly), then their fee award would be reduced on a sliding-scale basis; the longer it took to achieve their client's consent, the less their fee award.[121] Without the consent of all 587, no one would receive anything.[122] Thus, according to the Second Circuit, by entering into this agreement with the defendant, plaintiffs' law firm "violated its duty to advise and represent each client individually, giving due consideration to differing claims, differing strength of those claims, and differing interests in one or more proper tribunals in which to assert those claims."[123]

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[114] *Gallion*, 266 S.W.3d at 803-04. The New York fen-phen settlement by Napoli, Kaiser & Bern was likewise subject to extensive ethical review and a judge ultimately concluded that "a sufficient showing has been made that the Napoli Firm may have violated the Disciplinary Rules and may have made material misrepresentations in the Letter and the Form of Acceptance." Appel-Hole v. Wyeth-Ayerst Labs. (*In re* N.Y. Diet Drug Litig.), No. 700000/98, 2007 WL 969426, at *11 (N.Y. Sup. Ct. Mar. 27, 2007).

[115] *Gallion* 266 S.W.3d at 803-04.

[116] Erichson, *supra* note 25, at 986.

[117] For example, Wally Figg's antics come readily to mind. JOHN GRISHAM, THE LITIGATORS (2011).

[118] 660 F.3d 131 (2d Cir. 2011).

[119] *Id.* at 134-35.

[120] *Id.*

[121] *Id.* at 139.

[122] *Id.*

[123] *Id.*

Although Rule 23's effectiveness in fashioning a judicial surrogate to protect absent class members is open to debate,[124] when that protective layer disappears—as it does in nonclass aggregation—the problems metastasize. The agency problems remain, but the judge no longer has clear authority to get involved and counsel's ethical obligations to the group are muddied by traditional ethical rules that assume individual client monitoring.[125] Yet, when multiple claimants exist, plaintiffs' attorneys face enormous pressure to tender finality to the defendant; that is, after all, what ultimately what dictates the lawsuit's success. But the quest to achieve that finality outside the well-traveled class-action path spurs unethical behavior. And tying the lawyer's payday to the settlement—as the contingent fee does—only adds fuel to this fire. In short, this shift toward nonclass aggregation presents a striking need for someone, somehow to monitor the litigation and the attorneys on the plaintiffs' behalf.

II. ALTERNATIVE LITIGATION FINANCING

The agency problems in aggregate litigation and the lack of a viable monitor portend an alliance of unseemly bedfellows and troublesome trade-offs. In a near-perfect world,[126] each individual would be able to pursue the full value of her claim, no matter how small, and perhaps even avoid the transaction costs associated with attorneys' fees. The plaintiff would be eminently rationale, swayed neither by the shrewd framing of settlement options, nor by the press of mortgage payments or medical bills, nor even by inexperience or informational asymmetries.[127] But this is not the world we live in. Nor is our world one in which judges can continue to act as fiduciaries for the group, gingerly watching out for plaintiffs' best interests should their agent's incentives stray from theirs. The world we live in is one in which the would-have-been class action often lies still-born at the hands of the judge, driving

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[124] *See, e.g.*, William B. Rubenstein, *The Fairness Hearing: Adversarial and Regulatory Approaches*, 53 UCLA L. REV. 1435, 1445 (2006) (observing that judges "suffer from a remarkable informational deficit in the fairness-hearing process"); Adam S. Zimmerman & David M. Jaros, *The Criminal Class Action*, 159 U. Pa. L. Rev. 1385, 1429-30 (2011) (observing that "commentators have questioned the effectiveness of judicial review in class action settlements," but that courts can demand that parties "explain the complex trade-offs they have made in arriving at a settlement, and require a reasonable decision-making process when they arrive at a distribution that affects restitution to thousands of potential victims.")

[125] *See, e.g.*, *id.* at 140 ("First, because LMB was not lead counsel in a class action, the class-protective provisions of Rule 23 were not triggered.").

[126] Obviously, in a perfect world, torts would never occur, people would honor their contractual obligations, and property would pass blissfully from one owner to the next without ever having been trespassed or infringed upon by another.

[127] *See generally* Adam Zimmerman, *Funding Irrationality*, 59 DUKE L.J. 1105, 1109-11 (2010) (describing the cognitive biases that affect plaintiffs' settlement decisions in large-scale litigation).

the potentially wayward agent to either abandon the endeavor altogether or to recruit and represent hundreds of roughly similarly situated clients with no hope of establishing a meaningful attorney-client relationship.

Enter then the trade-offs: the third-party financiers hoping to turn a profit off of others' misfortune versus the palpable need for continued access to the lawyers, to the courthouse, to justice; the questions about decisional control that pit paternalism against autonomy; and the ethical concerns raised when someone other than the client has a say versus the dire need for attorney oversight. And these trade-offs are but the tip of the iceberg. Underlying each is a host of issues that range from the practical—whether clients can give informed consent to allow financiers to share in their proceeds—to the convoluted—such as the myriad, mixed incentives that result when a new entity enters into an already complex principal-agent dynamic. Further still, these knotty questions say nothing about what will become of cases in which clients principally want declaratory or injunctive relief—cases that third-party funders have no incentive to fund. This section begins to untangle these issues by demystifying the types of alternative litigation financing presently available and tracing the incentives of financiers, plaintiffs, and plaintiffs' lawyers. The next Part then considers whether third-party financing might actually help alleviate the agency problems that arise in aggregate litigation by shouldering litigation costs and providing a much needed monitor.

A. A Taxonomy of Third Party Financing

Presently, there are three main types of third-party financing—consumer legal funding, loans to plaintiffs' law firms, and commercial dispute funding—each of which raise distinct legal and ethical concerns. Third-party funding, or "alternative litigation financing," started in Australia, made its way to the United Kingdom,[128] and took root in the United States when companies started loaning money to cash-strapped plaintiffs who could not use their lawsuit as bank collateral, but needed money for day-to-day expenses. This so-called "*consumer legal funding*" is a nonrecourse loan where a litigant would not need to pay any more than what she receives from the lawsuit; there is no personal liability—if she loses the suit, the lender loses the money.[129] Given the risk involved, however, interest rates can be

[128] Nate Raymond, *More Attorneys Exploring Third-Party Litigation Funding*, N.Y. L.J., June 4, 2010. Australia does not allow contingency fees, but roughly five investment firms fill the void. Susan Lorde Martin, *Litigation Financing: Another Subprime Industry That Has a Place in the United States Market*, 53 VILL. L. REV. 83, 107 (2008).

[129] STEVEN GARBER, RAND CORP., ALTERNATIVE LITIGATION FINANCING IN THE UNITED STATES: ISSUES, KNOWNS, AND UNKNOWNS 10 (2010); *What is Legal Finance?*, AM. LEGAL FIN. ASSOC., http://www.americanlegalfin.com/alfa1/LinkClick.aspx?fileticket=1Ia9qsxV0eQ%3d&tabid=71&mid=553.

quite high—between 36 and 150 percent per year—but the nonrecourse basis enables funders to avoid state usury laws.[130] Consumer legal funders making cash advances to plaintiffs traditionally run up against historical maintenance doctrines, which prohibit third parties from assisting a litigant in pursing a lawsuit.[131]

Over time, a second type of financing emerged: *loaning money to plaintiffs' law firms*, as opposed to cash-advance loans to plaintiffs themselves, is a growing market among a niche practice. As of early 2010, only around nine companies provided loans to law firms, but as of late 2011, that number had grown to around twelve.[132] When financiers lend money to law firms, they secure those debts not by a single case, but by all of the firm's assets, including future fee awards from other cases. Occasionally, funders will lend lawyers money based on a trial verdict on appeal.[133] Unlike a nonrecourse loan, plaintiffs' firms must repay the money regardless of whether they win or lose a particular case.[134] Such was the case in financing the ground zero workers' litigation; Napoli Bern would have to reimburse Counsel Financial regardless of the case's outcome.[135] Interest rates are significantly higher than what a bank might charge for a loan based on traditional assets—rates tend to be "north of 20 percent"—which makes the loans unattractive to well-financed firms.[136] Still, lenders in this area can do what banks can't; banks loan money based on traditional assets and collateral, not on potential winnings.[137]

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[130] Kirby Griffis, *Follow the Money: Litigation Funders Back Your Foes*, METROPOLITAN CORP. COUNS., July 15, 2011, at 1.

[131] Osprey, Inc. v. Cabana Ltd. P'ship, 532 S.E.2d 269, 273 (S.C. 2000).

[132] Steven Garber lists nine companies that loaned money to plaintiffs' law firms in early 2010, including Advanced Legal Capital, Advocate Capital, Inc., Counsel Financial, Evergreen Funding Group, LawFinance Group, Inc., Oxbridge Financial Group LLC, Rapid Funds, RD Legal Capital, and ViaLegal Funding. Garber, *supra* note 129, at 14. Several other companies now exist, including Amicus Capital Services, LLC, http://www.wdtconsulting.com/law-firm-loans.html ("We offer loans secured by your portfolio of cases, for four to five times more money than a traditional bank could offer."); BridgePoint Financial Services, http://www.bpfin.com/personal-injury/disbursement-financing/index.html ("We recognize that personal injury law firms are capital intensive businesses with unique cash flow cycles relative to other professional service providers."); LawsuitLoanHQ, http://lawsuitloanhq.com/plaintiff-case-costs.htm (Trimark Capital Funding, Inc.) ("We are experts in legal finance, lawsuit loans, law firm cash flow financing, attorney funding, law firm loans and legal practice line of credit.").

[133] Alison Frankel, *Helping Underfunded Plaintiffs Lawyers—At a Price*, LAW.COM, Feb. 13, 2006, http://www.law.com/jsp/law/international/LawArticleFriendlyIntl.jsp?id=900005547685.

[134] Garber, *supra* note 129, at 10.

[135] Goldstein & Edelman, *supra* note 14.

[136] Frankel, *supra* note 133.

[137] As LawFinance prominently explains in its slogan, "We Do What Banks Won't." LAWFINANCE GRP., http://www.lawfinance.com/ (last visited Feb. 5, 2012).

Finally, a burgeoning market of around seven lenders provide money directly to businesses to finance *commercial, business-versus-business disputes* in exchange for either a percentage of the plaintiff's eventual recovery or a multiple of the supplied capital.[138] Those percentages range from 35-67 percent of the lawsuit's recovery.[139] This kind of lending may run into historical prohibitions on champerty, a form of maintenance where the lender receives an interest in the suit's outcome.[140] Two of the lenders in this area, Juridica Investments and Burford Capital, Ltd. are publicly traded companies in the Alternative Investment Market on the London Stock Exchange, and principally bankroll international arbitrations, intellectual property, breach of contract, and antitrust disputes.[141] Most commercial dispute lenders currently steer clear of funding aggregate litigation and leave those investments to funders who loan money to plaintiffs' law firms. But, as the following sections explore, this model of contracting with the plaintiffs for a portion of their proceeds has the most potential for creating a workable monitor.[142] And for those investors seeking a longer-term investment with a potentially exponential payoff, funding aggregate litigation is a logical next step.

B. Mixed Litigation and Investment Incentives

Finding a viable intermediary entails paying careful attention to financiers' incentives and the ways in which those incentives dovetail with plaintiffs' aims and

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[138] Garber, *supra* note 129, at 13 (such lenders include ARCA Capital, Burford Capital, Calunius Capital, IMF, Juridica Investments, and Juris Capital); Hamerman, *supra* note 56; Vanessa O'Connell, *Funds Spring Up to Invest in High-Stakes Litigation*, WALL ST. J., Oct. 3, 2011, at B1 ("At least three start-up business are entering the fledgling 'alternative litigation funding' market this year, creating funds that will invest at least a few million dollars in a case in exchange for a share of the lawsuit's winnings, which can be in the several-million-dollar or even billion-dollar range."); BLACKROBE CAPITAL, http://www.blackrobecapital.com (last visited Feb. 5, 2012) (noting that BlackRobe Capital was founded, in part, by Tim Scrantom, who also began Juridica).

[139] Raymond, *supra* note 128.

[140] Osprey, Inc. v. Cabana Ltd. P'ship, 532 S.E.2d 269, 273 (S.C. 2000) ("[P]ut simply, maintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty.").

[141] *See* Garber, *supra* note 129, at 13; Hamerman, *supra* note 56; Raymond, *supra* note 128; Burford Grp. LLC, *Submission of Burford Group LLC on the Working Group's Issue Paper Concerning Alternative Litigation Financing*, ABA COMM'N ON ETHICS 20/20, 2 (Feb. 15, 2011), http://www.americanbar.org/content/dam/aba/migrated/2011_build/ethics_2020/comments_on_alternative_litigation_financing_issues_paper.authcheckdam.pdf ("Burford Group carries on its activities in the United States through its subsidiary, Burford Group LLC.").

[142] Burford Capital, Ltd. is, however, currently funding the Ecuadorian personal-injury litigation against Chevron, which involves thousands of plaintiffs. Hurley, *supra* note 14. James Tyrrell, Jr., the Ecuadorian plaintiffs' attorney also acts as outside counsel to both Burford and Juridica. Raymond, *supra* note 128.

public-enforcement goals. These interests hinge on litigation's two primary functions: (1) resolving disputes and (2) preventing disputes by defining, shaping, and clarifying the law to make behavioral modification and compliance possible.[143] One might reframe this dichotomy as compensating, or making "whole" in some sense a wronged party and deterring wrongful or negligent conduct from occurring. Preventing disputes relies on litigants to push, shape, and define legal ambiguities through arguments and establishing precedent. Yet, there is somewhat of a conflict between dispute-resolution goals and deterrence aims: if the settlement offer is generous enough to buy the plaintiff off, she has little incentive not to accept it and to push for further judicial rulings and appeals.[144] Repeat players, however, like nonprofit groups, attorneys, funders, and defendants, have at least some impetus to invest in setting precedent and clarifying laws.[145] Although funders are repeat players, many would prefer a quick settlement and an expeditious investment return.

The following analysis of parties' incentives assumes that each entity—plaintiffs, their attorneys, and funders—is separate. Part III then considers how mixing these incentives by allowing financiers to fund aggregate litigation could change and distort them. Note too that special ethical issues may arise on the very rare occasion when the plaintiffs' attorney is also an investor in or affiliated with the third-party funder.[146] For example, prominent defense attorney James Tyrrell, Jr., a partner at Patton Boggs, is outside counsel to both Juridica and Burford.[147] He is also the attorney for the Ecuadorian plaintiffs in their headline-making case against Chevron, which Burford funds.[148]

1. Plaintiffs' Incentives

Nonclass aggregation adds a new wrinkle in evaluating plaintiffs' litigation aims. In class actions, dealing with plaintiffs who are largely absent and typically disinterested is a much simpler proposition than managing hundreds or thousands of clients whose goals do not always align with each others' or their attorneys'.

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[143] *See generally* Robert G. Bone, *Lon Fuller's Theory of Adjudication and the False Dichotomy Between Dispute Resolution and Public Law Models of Litigation*, 75 B.U. L. REV. 1273, 1296-1304 (1995) (discussing litigation's function).

[144] David Luban, *Settlements and the Erosion of the Public Realm*, 83 GEO. L.J. 2619, 2623 (1995); Richard H. McAdams, *The Expressive Power of Adjudication*, 2005 U. ILL. L. REV. 1043, 1114-16; William M. Landes & Richard A. Posner, *Adjudication as a Private Good*, 8 J. LEGAL STUD. 235, 238 (1979)

[145] KRITZER, *supra* note 71, at 16; Maya Steinitz, *Whose Claim Is This Anyway? Third-Party Litigation Funding*, 95 MINN. L. REV. 1268, 1312-13 (2011).

[146] For some guidance on these issues, see ABA Comm'n on Ethics 20/20, White Paper on Alternative Litigation Finance 17-20 (2011) (unpublished draft) (on file with author); *see also* MODEL RULES OF PROF'L CONDUCT R. 1.7(a)(2), 1.8(e), 1.8(i) (2011).

[147] Raymond, *supra* note 128.

[148] Hurley, *supra* note 14.

Plaintiffs' litigation incentives do not fit easily within a single box. Consider a few examples: a woman paralyzed in a rollover accident demanded that Ford and Firestone broadcast a videotaped apology to settle, Paula Jones demanded but never received an apology from President Clinton, and many of the September 11 victims wanted information about the facts and circumstances, to hold those responsible accountable, to publicly condemn wrongdoing, and to do something that would promote change.[149]

When asked why they litigated, plaintiffs with tort claims such as medical injuries insisted that they were litigating on principle, not for the money.[150] Their aims "were largely composed of extra-legal objectives of principle, with 41% not mentioning monetary compensation at all, 35% saying it was of secondary importance, 18% describing money as their primary objective in suing, and only one person (6%) saying it was money alone."[151] Plaintiffs litigate to establish precedent, express their feelings, have the defendant admit fault and responsibility, ensure that the event will never happen again, reveal cover-ups, discover answers, punish or gain retribution, receive an apology, obtain dignity and respect post-injury, and be heard.[152] Consequently, as Part IV explores, financially motivated third-party financiers are not always the right solution for all plaintiffs, though plaintiffs' attorneys working on a contingency fee have long monetized these claims.

When, whether, and under what terms to settle may not be a rational choice for most plaintiffs. In making settlement decisions, plaintiffs may fall prey to contrast

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[149] Erin Ann O'Hara & Douglas Yarn, *On Apology and Consilience*, 77 WASH. L. REV. 1121, 1125 (2002); Gillian K. Hadfield, *Framing the Choice Between Cash and the Courthouse: Experiences with the 9/11 Victim Compensation Fund*, 42 LAW & SOC'Y REV. 645, 649 (2008); Deborah R. Hensler, *Money Talks: Searching for Justice Through Compensation for Personal Injury and Death*, 53 DEPAUL L. REV. 417, 449 (2003).

[150] Tamara Relis, *"It's Not About the Money!": A Theory of Misconceptions of Plaintiffs' Litigation Aims*, 68 U. PITT. L. REV. 701, 721 (2007).

[151] *Id.* at 723.

[152] *Id.* at 722-23 & fig. 4. Other studies confirm these results. *E.g.*, Randall P. Bezanson, *The Libel Suit in Retrospect: What Plaintiffs Want and What Plaintiffs Get*, 74 CALIF. L. REV. 789, 799 (1986); Marc Galanter, *Adjudication, Litigation, and Related Phenomena*, *in* LAW AND THE SOCIAL SCIENCES 151, 191 (Leon et al., eds., 1986); Marc Galanter, *Reading the Landscape of Disputes: What We Know and Don't Know (and Think We Know) About Our Allegedly Contentious and Litigious Society*, 31 UCLA L. REV. 4, 30-31 (1983); Hazel Genn, *Access to Just Settlements: The Case of Medical Negligence*, *in* REFORM OF CIVIL PROCEDURE: ESSAYS ON "ACCESS TO JUSTICE" (A. Zuckerman & R. Cranston eds., 1995); Deborah R. Hensler, *Resolving Mass Toxic Torts: Myths and Realities*, 1989 U. ILL. L. REV. 89, 99; Gerald B. Hickson et al., *Factors that Prompted Families to File Medical Malpractice Claims Following Perinatal Injuries*, 267 JAMA 1359, 1361, 1367 (1992); Allan Lind et al., *In the Eye of the Beholder: Tort Litigants' Evaluations of their Experiences in the Civil Justice System*, 24 LAW & SOC'Y REV. 953, 965-67 (1990); Sally Engle Merry & Susan S. Silbey, *What Do Plaintiffs Want? Reexamining the Concept of Dispute*, 9 JUST. SYS. J. 151, 153 (1984); O'Hara & Yarn, *supra* note 149, at 1125; *Tom R. Tyler, A Psychological Perspective on the Settlement of Mass Tort Claims*, 53 LAW & CONTEMP. PROBS. 199, 204 (1990). *But see* RICHARD LEMPERT & JOSEPH SANDERS, AN INVITATION TO LAW AND SOCIAL SCIENCE 175 (1986) (concluding that plaintiffs other than those involved in discrimination lawsuits were principally concerned about economic well-being).

bias, tendencies toward risk aversion, and group decisionmaking biases, such as confirmation bias and group polarization. First, contrast bias affects the way plaintiffs evaluate settlement options depending on what other options are offered to them simultaneously and how many choices they have.[153] For instance, people tend to decide more quickly if an offer includes only a single option as opposed to two attractive choices, regardless of whether both options leave the decisionmaker better off; and adding in a third inferior option makes an already available choice appear even more attractive than it otherwise would.[154] Although frank legal advice diminishes this bias,[155] the circumstances of nonclass aggregation make candid advice improbable.[156] Aggregated clients have attenuated relationships with their attorneys and lawyers' self-interest as financiers may color their substantive advice.[157]

Second, risk preferences may affect plaintiffs' decisionmaking in ways that differ from the risk preferences of their attorneys or third-party financiers. Research shows that cognitive psychological factors like framing,[158] anchoring, and equity-seeking[159] affected plaintiffs' risk preferences more so than they did their attorneys'.[160] In contrast, their attorneys' desire to settle was animated principally by

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[153] Mark Kelman et al., *Context-Dependent in Legal Decision Making*, 25 J. LEGAL STUD. 287, 297-300 (1996); Zimmerman, *supra* note 127, at 1142-49; *see also* Mark Kelman, Yuval Rottenstreich & Amos Tversky, *Context-Dependence in Legal Decision Making*, 25 J. LEGAL STUD. 287, 288-89 (1996); Russell Korobkin & Chris Gutherie, *Psychological Barriers to Litigation Settlement: An Experimental Approach*, 9 MICH. L. REV. 107, 129-42 (1994) (noting the effects of frames and anchors).

[154] DAN ARIELY, PREDICTABLY IRRATIONAL: THE HIDDEN FORCES THAT SHAPE OUR DECISIONS 10–15 (2008); Chris Guthrie, *Panacea or Pandora's Box?: The Costs of Options in Negotiation*, 88 IOWA L. REV. 601, 619 (2003); Zimmerman, *supra* note 127, at 1143-45; *see also* Ravi Dhr, *Consumer Preference for a No-Choice Option*, 24 J. CONSUMER RES. 215, 229 (1997); Joel Huber, John W. Payne & Christopher Puto, *Adding Asymmetrically Dominated Alternatives: Violations of Regularity and the Similarity Hypothesis*, 9 J. CONSUMER RES. 90, 94 (1982); Sanjay Mishra, U.N. Umesh & Donald E. Stem, Jr., *Antecedents of the Attraction Effect: An Information-Processing Approach*, 30 J. MARKETING RES. 331, 332–35 (1993); Simone Moran & Joachim Meyer, *Using Context Effects to Increase a Leader's Advantage: What Set of Alternatives Should be Included in the Comparison Set?*, 23 INT'L J. RES. MARKETING 141 (2006); Eldar Shafir, Itamar Simonson & Amos Tversky, *Reason-Based Choice*, *in* CHOICES, VALUES, AND FRAMES 607-08 (Daniel Kahneman & Amos Tversky eds., 2000).

[155] Russell Korobkin & Chris Gutherie, *Psychology, Economics, and Settlement: A New Look at the Role of the Lawyer*, 76 TEX. L. REV. 77, 82 (1997); Zimmerman, *supra* note 127, at 1146.

[156] *See supra* Part II.C.

[157] Zimmerman, *supra* note 127, at 1146 n.186; *see generally* Korobkin & Gutherie, *supra* note 155, at 124.

[158] *See* Korobkin & Gutherie, *supra* note 153, at 109, 129-31 ("People avoid risk when they choose between options they understand as gains, but they prefer risk when they select between choices viewed as losses.").

[159] *See id.* at 109 ("People want what they are legally entitled to, but they also want recognition of their claim's validity.").

[160] Korobkin & Gutherie, *supra* note 155, at 124; Korobkin & Gutherie, *supra* note 153, at 111.

financial calculations.[161] Because trial is particularly expensive for a contingent-fee lawyer, she is likely to favor settlement more often than her clients, who may be more affected by contrast bias, initial settlement offers (anchoring effects), or nonmonetary motivations.[162] Disparate risk preferences also mean that settlements may not reflect the merits so much as the plaintiff's (or her attorney's) risk tolerance.[163] This can result in sub-optimal deterrence for defendants who take calculated financial risks and thereby undermine one of litigation's public functions.

Risk preferences are likewise affected by how much money is at stake vis-à-vis a person's overall wealth; people tend to be more willing risk takers when less money is at stake.[164] This so-called "peanuts effect," where people take risks when playing for "peanuts," suggests that interested parties with less at stake will be less risk averse when litigating.[165] So, in a negative-value case like a consumer suit, the contingent-fee lawyer with a substantial stake in the whole litigation is likely more risk averse than her clients; but when the stakes are higher—as in personal-injury or products-liability cases—risk preferences may align. A middle-class plaintiff with a claim worth a few hundred thousand dollars, a contingent-fee attorney, and even a third-party financier with a substantial investment in the case's outcome may all be similarly risk averse. But a plaintiff who litigates for nonmonetary reasons, like revealing cover-ups or wanting to punish the defendant, may have a higher risk tolerance, as might a lawyer for whom the lawsuit is as much about creating or maintaining a certain reputation (say, for large settlements or jury awards) as it is about a particular fee.[166]

Third, the risk-seeking versus risk-avoiding dynamic changes further when decisionmaking is no longer an individual endeavor, but requires group consensus as aggregate litigation frequently does. As I have explored in the past,[167] interpersonal group dynamics require heightened sensitivity to the decisionmaking process as part

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[161] Korobkin & Gutherie, *supra* note 155, at 124.

[162] *See id.*

[163] Molot, *supra* note 16, at 70.

[164] Harry Markowitz, *The Utility of Wealth*, 60 J. POL. ECON. 151, 151 (1952); Drazen Prelec & George Lowenstein, *Decision Making Over Time and Under Uncertainty: A Common Approach*, 37 MGMT. SCI. 770 (1991); Bethany J. Weber & Gretchen B. Chapman, *Playing for Peanuts: Why Is Risk Seeking More Common for Low-Stakes Gambles?*, ORG. BEHAV. & HUM. DECISION PROCESSES, May 2005, at 31, 31-33.

[165] *See* Michael Gousgounis, Association-Driven Aggregate Litigation: Peanuts Effect and Democratization of Litigation Governance 5 (May 1, 2009) (unpublished manuscript), *available at* http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1469046.

[166] KRITZER, *supra* note 71, at 219-22.

[167] Burch, *supra* note 80, at 506; Elizabeth Chamblee Burch, *Group Consensus, Individual Consent*, 79 GEO. WASH. L. REV. 506 (2011) [hereinafter Burch, *Group Consensus*]; Elizabeth Chamblee Burch, *Litigating Groups*, 61 ALA. L. REV. 1 (2009).

and parcel of litigation procedures.[168] As plaintiffs participate and deliberate in group governance, they tend to influence one another's decisions, for better or worse. If group norms stifle dissent among homogenous group members, then members' convictions can make them discount contrary evidence (confirmation bias) or move toward extreme positions (group polarization).[169] Cohesive groups, however, might incur moral obligations of solidarity and loyalty to one another, which means that they may ultimately push for a settlement that is in the best interests of the group as a whole.[170] So long as the cohesive group incorporates diverse viewpoints (such as those of their attorneys, other plaintiff groups, or a third-party financier) into their discussion and decisionmaking processes, they can avoid group decisionmaking's most detrimental effects.[171]

2. Plaintiffs' Attorneys' Incentives

Plaintiffs are not the only ones subject to various biases in decisionmaking; their lawyers are equally vulnerable, but in different ways. The principal-agent literature explored in Part I.B exposes the basic economic problem and discusses attorneys' financial interests, but only partially explains attorneys' incentives. Although lawyers are less subject to contrast biases and emotional tugs, they are not always solely motivated by financial calculations. As repeat players, attorneys' reputations among the plaintiffs' bar, defense attorneys, and clients matter for referrals, maintaining credible threats, encouraging repeat business, and achieving favorable settlements.[172] An attorney's reputation may thus function as an economic control on potential self-dealing and collusive or quick-pay settlements.[173] Likewise, settlement quality is heavily intertwined with the lawyer's reputation and her ability to pose a plausible threat to defendants through accepting meritorious cases, having the resources available for case preparation and trial, and making justifiable settlement demands.[174]

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[168] I do not mean that litigation is truncated in terms of time to settlement, but that aggregate litigation lacks the traditional progression toward trial that an individual litigant might experience.

[169] Elizabeth Chamblee Burch, *Optimal Lead Plaintiffs*, 64 VAND. L. REV. 1109, 1152-54 (2011); *see also* Dieter Frey, *Recent Research on Selective Exposure to Information*, *in* ADVANCES IN EXPERIMENTAL SOCIAL PSYCHOLOGY 41, 52-53 (Leonard Berkowitz ed., 1986); Joshua Klayman, *Varieties of Confirmation Bias*, *in* DECISION MAKING FROM A COGNITIVE PERSPECTIVE 385, 385-87, 398 (Jerome Busemeyer & Reid Hastie, eds. 1995); Raymond S. Nickerson, *Confirmation Bias: A Ubiquitous Phenomenon in Many Guises*, 2 REV. GEN. PSYCHOL. 175, 178, 210 (1998); Stefan Schulz-Hardt et al., *Biased Information Search in Group Decision Making*, 78 J. PERSONALITY & SOC. PSYCHOL. 655, 656-58 (2000).

[170] Burch, *Group Consensus*, *supra* note 167, at 519-23.

[171] Burch, *supra* note 80, at 117-25.

[172] KRITZER, *supra* note 71, at 232-39.

[173] *Id.* at 221-22; Korobkin & Gutherie, *supra* note 155, at 123.

[174] KRITZER, *supra* note 71, at 242.

Having the resources to craft a reputation as a serious attorney who gets results is far more difficult in the current economic climate. Consequently, plaintiffs' attorneys are more likely to turn to nontraditional funding sources for four reasons. First, recall that the fixed costs of aggregate litigation, as opposed to a class action, are likely to increase substantially. Not only must lawyers spend the same resources on developing generic assets like scientific research and expert analysis, they must also pour money into advertising, client recruitment, client counseling, filing fees, and the administrative costs of keeping up with each client's documents.

Second, because plaintiffs' attorneys work on a contingent fee or must prevail before the judge awards them fees under a fee-shifting statute, they frequently encounter cash-flow problems. This can bring them close to insolvency and impact their ability to accept new cases, invest sufficient resources in current cases, and compete with more established law firms.[175] Cash-flow problems likewise undermine their ability to pose a credible threat to the defendant, which usually has far more resources and leverages its superior economic position in hopes of pressuring plaintiffs to accept a low-ball offer. Third, the economic downturn and tightened lending standards have all but dried up traditional funding sources like banks,[176] which drives the ever-entrepreneurial and ever-creative lawyer to seek nontraditional funding. Finally, even the financially solvent firm might seek alternative funding to fortify its threat to the defendant. Because funders conduct their own due diligence to assess the case's merits, if funding is disclosed, it sends both parties an additional signal about the value of plaintiffs' claims.[177]

3. Financiers' Incentives

Financiers' investment incentives are relatively simple: they want to make money and are willing to take significant risks for significant returns, at least so long as they do not exhaust their capital along the way.[178] That simple incentive, however, belies the complexity that animates it. Take settlement, for example: commercial-claims lenders tend to invest in lawsuits that may settle quickly so they can collect their share and move on to other ventures, but funders who loan money to plaintiffs' law firms or to plaintiffs themselves based on hefty annual interest rates may want to

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[175] Garber, *supra* note 129, at 23.

[176] Alexa Hyland, *Firms Make Case for Legal Loans*, L.A. BUS. J., April 21, 2008, at A1.

[177] *See* Telis Demos, *Cashing In on Litigation*, FORTUNE, May 4, 2009; Garber, *supra* note 129, at 24, 32-33; Max Schanzenbach & David Dana, How Would Third Party Financing Change the Face of American Tort Litigation? The Role of Agency Costs in the Attorney-Client Relationship 12 (Sept. 24, 2009) (unpublished manuscript), *available at* http://www.law.northwestern.edu/searlecenter/papers/Schanzenbach_Agency%20Costs.pdf. As Garber suggests, this is far from a straightforward proposition and it raises substantial questions for game theorists.

[178] Garber, *supra* note 129, at 24.

delay settlement to increase those charges.[179] And no lender is concerned with equitable or injunctive relief.

Incentives vary depending on the investment and the investment strategy. So, financiers backing commercial, business-dispute claims will have different incentives than those who loan money to plaintiffs' law firms, for example. When investors bankroll commercial, business-versus-business claims in exchange for a share of the eventual recovery, they tend to avoid cases that involve novel legal questions or that could end up in a jury trial.[180] Juries inject too much uncertainty into the process, as do politically charged cases.[181] For similar reasons, these investors avoid cases likely to be appealed or where the opposing party lacks deep pockets.[182]

Richard Fields, the CEO of Juridica Capital Management, a company that trades on the London Stock Exchange but invests mostly in commercial claims within the United States, explained that his company funded only 17 out of 122 potential cases last year.[183] Selecting cases involved a "two-month due diligence process that examine[d] credit risk, potential profit and expenditure, defendants' financial status

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[179] *See generally* Terry Carter, *Cash Up Front*, ABA JOURNAL, Oct. 2004, http://www.abajournal.com/magazine/article/cash_up_front ("[C]ash advances go to plaintiffs before trial or settlement, with monthly interest rates ranging form 2 percent to 4 percent in some states to more than 6 percent in Texas, 8 percent in California, and as high as 15 percent in Nevada. These rates sometimes are compounded and can approach 200 percent annually."); Ben Hallman, *ABA Still Studying Ethical Issues Raised by Hedge Funds, Others Investing in Lawsuits*, CTR. FOR PUB. INTEGRITY, June 16, 2011, http://www.iwatchnews.org/2011/06/16/4935/impact-influential-ny-ethics-panel-cautions-lawyers-dealings-lawsuit-funding. *But see* William J. Gorta, *Bitten by Lawsuit 'Sharks,'* N.Y. POST, Dec. 12, 2011, http://www.nypost.com/p/news/local/brooklyn/bitten_by_lawsuit_sharks_50H1EYevFanwCmIFBzgsWM (describing a $4,000 loan that morphed into $116,000 with interest and fees and, before settlement, the judge threatened to rule that the practice was usurious and unconscionable). As this example shows, even consumer funders might prefer to receive a quick turnaround on their investment.

[180] Jonathan D. Glater, *Investing in Lawsuits, for a Share of the Awards*, N.Y. TIMES, June 3, 2009, at B1 (interviewing Richard Fields, the CEO of Juridica Capital Management). Both Juridica and Burford Capital Ltd. invest in commercial disputes. Raymond, *supra* note 128.

[181] Glater, *supra* note 180, at B1.

[182] *Id.*; Hamerman, *supra* note 56 (quoting Mark Wells, CEO of Calunius Capital as saying, "Litigation could take many years and if, at the end of it, you're facing a company that can't get the assets to meet the claim, it's not very attractive.").

[183] Lauren Tara LaCapra, *Hedge Fund Hell: These Funds Sue You*, THE STREET, Jan. 23, 2009, http://www.thestreet.com/story/10459369/1/hedge-fund-hell-these-funds-sue-you.html?puc=_tscrss; Raymond, *supra* note 128; *Litigation Funding Services Enter United States*, LAW FIRM MGMT., July 2009 (Juridica has raised more than $100 million in investment capital and financed 17 separate matters, mostly in the United States."); Hamerman, *supra* note 56.

and other players involved in the case."[184] He spreads investments across substantive areas, such as intellectual property, price-fixing, and shareholder disputes and noted, "90% of cases [were] settled without a lengthy trial or resolved through motions," which allowed "for a quick turnaround on profit when the right case is selected."[185] Commercial-claims lenders hope that the pickiness with which they conduct their due diligence and their selectivity will "send[] a powerful message to the opposing side with respect to the likely outcomes, thus encouraging settlements."[186] Consequently, they accept cases with quality lawyers who have a proven success rate.

When lenders loan plaintiffs' law firms money, however, their incentives align more with the law firm than the client. Because recourse loans are secured by all of the law firm's assets, financiers' due diligence concentrates less on the particulars of any one case and more on the firm's portfolio of cases and overall financial stability.[187] Of course, law firms that heavily invest in a particular type of aggregate litigation (say, Accutane, Vioxx, or Zyprexa) would be different. Investing in a firm like Napoli Bern, which had substantial capital tied up in one principal case with many clients—the ground zero workers—would require risk assessments more akin to those conducted by Richard Fields of Juridica. As two New York Times investigative reporters explain:

> Lenders employ experienced lawyers to judge the strength of cases. They consult databases showing the results of similar lawsuits, just as appraisers value homes based on recent sales. A corporate defendant may have a history of battling personal injury claims; or juries in a specific county may have a history of siding with local employers. Then they place their bets. Counsel [Financial] will invest up to $10 million in a law firm.[188]

For instance, before Oxbridge Financial Group loaned money to Jared Woodfill for his lawsuits against BNSF Railway, the group "spent several months reviewing the cases" and sent "lawyers to Texas to look at documents and to question Woodfill and his partners."[189] Because law firms are on the hook regardless of the case's outcome, they have more incentive to negotiate lower interest rates.[190] Even still,

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[184] LaCapra, *supra* note 183; *see also* Burford Grp. LLC, *supra* note 141, at 5 ("Burford does extensive due diligence before financing a matter . . .").

[185] LaCapra, *supra* note 183.

[186] *Litigation Funding Services Enter United States*, L. FIRM MGMT., July 2009; *see also* Melissa Maleske, *Hedging Bets; As Litigation Activity Rises, Some U.S. Hedge Funds Are Investing in Corporate Lawsuits*, INSIDE COUNS., Dec. 7, 2009, http://www.insidecounsel.com/2009/12/01/hedging-bets.

[187] Frankel, *supra* note 133 (interviewing Gary Chodes, the CEO of Oasis Legal Finance Group, Michael Blum, the CEO and co-founder of LawFinance, and Paul Myers, the president of Advocate Capital).

[188] Ben Hallman & Binyamin Appelbaum, *Betting on Justice: Borrowing to Sue*, N.Y. TIMES, Nov. 15, 2010.

[189] *Id.*

[190] Goldstein & Edelman, *supra* note 14.

Oxbridge charges Woodfill around 16 percent annual interest, though that's less than the 18 percent that Counsel Financial charges and significantly less than what consumer funders charge plaintiffs.[191]

Consumer funders, who dispense nonrecourse loans to plaintiffs and thus risk losing money if the plaintiff loses the case, carefully evaluate the case's merits.[192] The danger, however, is that the plaintiff—knowing that she will be required to repay a minimum amount plus a percentage of the settlement—may refuse an otherwise reasonable offer and continue to trial. In one oft-cited case, a plaintiff borrowed $200,000 in exchange for agreeing to pay $600,000 plus half of any settlement, which led her to reason that proceeding to trial and losing would be a net gain unless a settlement offer exceeded $1.2 million.[193] She ultimately rejected a million-dollar settlement offer, revealed her rationale to her attorneys after trial, and her attorneys then sued the lender for fraud and tortious interference with their retainer agreement.[194]

Well aware of these risks, consumer funders aim to allot plaintiffs the ideal amount of money. As Dennis Shields, the president of LawCash, explains, "We want to give them enough money but also keep it on a tight rope" since a substantial advance could lead plaintiffs to decline early—but fair—settlements and take their chances at trial.[195] Likewise, too little money could lead plaintiffs to settle early—for many of the reasons that Owen Fiss identifies in *Against Settlement*—which would also decrease the funder's cut.[196]

Because procedural rules and substantive laws dictate monetary recovery (and thus the return on a third-party funder's investment), some financiers have reason to execute strategies that will change those rules and laws in ways that promote

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[191] Hallman & Appelbaum, *supra* note 188.

[192] Frankel, *supra* note 133 (interviewing Gary Chodes, the CEO of Oasis Legal Finance Group, Michael Blum, the CEO and co-founder of LawFinance, and Paul Myers, the president of Advocate Capital); Lawmax Legal Finance, http://www.fundmycase.com/en/attorney_info.php4 ("Any claim with good merits may qualify for funding. We typically require the following: compelling liability, defendant's ability to pay, documented damages.").

[193] Weaver, Bennett & Bland, P.A. v. Speedy Bucks, Inc., 162 F. Supp. 2d 448 (W.D.N.C. 2001) (denying defendant's motion to dismiss).

[194] *Id.*; Weaver, Bennett & Bland, P.A. v. Speedy Bucks, Inc., No. 1:00CV249, 2007 WL 2344820 (W.D.N.C. Aug. 14, 2007) (granting in part and denying in part plaintiff's motion for attorneys' fees and costs).

[195] Carter, *supra* note 179.

[196] Owen M. Fiss, *Against Settlement*, 93 YALE L.J. 1073, 1076-77 (1984) (explaining the ways in which resource disparities can influence settlement for economically disadvantaged plaintiffs); Carter, *supra* note 179.

recovery.[197] After all, like plaintiffs' and defense attorneys, they are repeat players. But this depends on the funder's investment strategy; if the strategy is to diversify its portfolio across substantive areas, as Richard Fields suggests is the case for commercial lenders, then there is less incentive to invest in rule changes. Commercial lenders seeking a quick profit are more likely to accept cases that avoid protracted appeals that rule changes may entail. In that way, they differ vastly from plaintiffs' attorneys who invested huge amounts of capital to promote legislation and set precedent in the asbestos and tobacco litigations.

Finally, financiers' fiduciary obligations run not to the plaintiff, as an attorney's duties do, but to their backers or shareholders.[198] When the company remains private, determining who the backers are—hedge funds, banks, and venture capitalists—is no easy feat. If news accounts are accurate, however, the investors are often passive in that they do not know where the money goes.[199] Yet, these alternative obligations may mean that funders, particularly publicly traded ones, would pressure plaintiffs to settle early so that they could report a higher quarterly profit.[200]

III. FINANCIERS AS INTERMEDIARIES

Layering a financier's incentives atop an already complex principal-agent relationship can fundamentally alter litigation and settlement dynamics. An investor who bankrolls a plaintiffs' law firm on a recourse basis and accrues monthly interest may care less about speedy settlements so long as the law firm's financial solvency is not in doubt. If the loan is nonrecourse in the same scenario, then both the funder and the lawyer have powerful incentives to settle quickly, perhaps at their clients' expense. But it is also possible to overlay the financier's incentives with the plaintiffs' incentives such that the financier, who has litigation expertise, sophistication, and substantial capital involved will monitor the attorney and thwart at least some of the agency problems that tend to arise between contingent-fee attorneys and their clients.

Still, the overlap is not perfect; there will inevitably be some slippage at the margins, which means that while funders' oversight can stymie certain unethical behaviors, it may exacerbate others. The financier is, after all, an intermediary with its own interests at stake and is less directly accountable to the plaintiffs than the

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[197] Steinitz, *supra* note 145, at 1312. Of course, funders may also finance corporate defendants, in which case the incentives differ.

[198] *Id.*

[199] Goldstein & Edelman, *supra* note 14.

[200] Steinitz, *supra* note 145, at 1319.

attorneys it oversees.[201] Nevertheless, financiers can play an important oversight role.

A. Revisiting the Missing-Monitor Problem: Unbundling Agency from Financing

Aligning financiers' incentives with plaintiffs' incentives requires them to become client-like by sharing a stake in the litigation's outcome. Just as the contingent fee partially assigns the attorney a portion of the plaintiff's proceeds, partially assigning the funder a percentage of the proceeds in exchange for financing the lawsuit on a nonrecourse basis makes that financier a super stakeholder.[202]

Allowing third parties like commercial-claims lenders to invest in the dispute's outcome by contracting directly with plaintiffs generates two principally positive effects. First, it disentangles—at least in part—the lawyer's role as investor from her role as a fiduciary and advisor. When litigating no longer threatens the law firm's solvency or ability to take on other matters, the attorney's loyalty no longer divides between self-preservation and the clients; she can afford to be a faithful representative. Second, assigning a financier a percentage of the plaintiffs' winnings converts that financier into a sizeable stakeholder and incentivizes it to monitor the attorneys and the litigation's costs. Because aggregate litigation is capital intensive, the investor can act as an advocate for the plaintiff by keeping costs reasonable. If the attorney wants to borrow money for travel and experts at a high interest rate, the investor has the incentive to prevent that transaction and finance those expenses at a much lower cost. And unlike geographically dispersed plaintiffs who face collective-action problems, a single, experienced financier can, for instance, require attorneys to keep their travel budgets reasonable.

But the need for monitoring and the degree to which agency is disentangled from risk depends chiefly on how the third-party financier compensates the lawyer for her services. Consider three options: (1) financiers pay the attorneys an hourly rate on the billable-hour system, (2) attorneys receive a discounted contingent fee that accounts for the lack of financial risk, or (3) financiers pay attorneys on a billable-hour rate plus some small percentage of the proceeds as a bonus.

1. Paying Plaintiffs' Attorneys on a Billable Hour System

Paying attorneys a billable-hour rate cleanly cleaves a lawyer's role as a risk-taking investor from her role as a client advisor and fiduciary, which means that she may be more loyal to her clients and have less incentive to arrange a quick settlement or collude with the defendant to settle on suboptimal terms. Moreover, a litigation-

[201] *See* Issacharoff & Ortiz, *supra* note 8, at 1645.

[202] For an alternative argument that plaintiffs should assign their full claim to a financier, see Schanzenbach & Dana, *supra* note 177, at 8-11.

savvy financier could negotiate a better hourly rate and thereby prevent astronomical fees while ensuring that the case is adequately funded.[203] Were a quick settlement offer generous enough to cover the financier's expenses and provide it with some return on the risk, the financier might push plaintiffs to accept the settlement, but here the billable-hour attorney's self-interest checks the financier's.[204] If anything, a billable-hour attorney would prefer to prolong the litigation, would advise plaintiffs to wait for a better deal, and would thus counterbalance the investor.

Billing hours also encourages lawyers to spend time counseling their clients about the alternative options available and explain the risks of litigating versus settling, which curtails the effect of contrast biases and uninformed risk preferences. This arrangement may likewise negate some of the pressure attorneys feel to cram the settlement down on their clients and misallocate settlement funds to payoff holdouts. When an attorney's payday isn't inherently tied to settling the lawsuit (as is the case when she works on a contingent fee), it alleviates her pressing financial concerns. So, though the attorney's ability to tender finality to the defendant is still vital for achieving a satisfactory settlement, she no longer feels the accompanying financial urgency and self-interest tugs that the current system engenders.

There are hazards involved with this billable-hour option, too. There is some risk that the billable-hour attorney would encourage her clients to accept a settlement that was not in their best interests if it furthers her prospects of doing repeat business with the financier. Thus, the collusion occurs not between plaintiffs' attorneys and defense attorneys, but between plaintiffs' attorneys and funders.[205]

But perhaps the most worrisome aspect of this compensation scheme is whether it would still attract the best and brightest plaintiffs' attorneys. Although defense attorneys on the billable-hour system make a very nice income, one rarely sees them with their own private planes and yachts, trappings common for successful mass-tort plaintiffs' attorneys. While third-party financing would increase competition among the plaintiffs' bar and may thus foster innovation and loyalty, the question remains whether plaintiffs would still receive advocacy of the same quality and creativity and whether trading some ingenuity for greater loyalty is worth the cost.

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[203] Subtracting the attorneys' fees from the funder's portion of the settlement proceeds would further incentivize scrutiny and oversight.

[204] *See* Coffee, *supra* note 28, at 342.

[205] *See infra* Part III.B.2. Collusion might occur in different forms, such as the financier paying the attorney a referral fee for clients. This would, of course, violate Rules 1.7(a)(2) and 7.2(b) of the Model Rules of Professional Conduct. A conflict also exists if the lawyer's interest "would materially impair [her] ability to consider alternative course of action that would otherwise be available to a client, to discuss all relevant aspects of the subject matter of the representation with the client, or otherwise provide effective representation . . ." RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 125 cmt. c (2011).

2. Financiers and Plaintiffs' Attorneys Split a Contingent Fee

This second option allows attorneys and financiers to split attorneys' standard contingent fee. The lawyers would receive a reduced award since they are shouldering less financial risk, but the payoff is still potentially momentous. This option recognizes that contingent fees and their attendant rewards encourage entrepreneurial attorneys to accept monolith cases and thus promote ex post law enforcement. It likewise accounts for the lingering reputational risks that attorneys must shoulder despite taking on less financial risk.

As noted, most claimants agree to a 33-to-40 percent contingent fee, though some judges have reduced that fee to between 25 and 28 percent.[206] Assuming the initial agreement's range provides ample incentive to accept the case's risks, the total percentage allocated to parties other than the plaintiffs should not exceed those parameters.[207] Attorneys and financiers might divide the total by splitting the percentage in some agreed upon fashion.

The trouble is, if both funders and attorneys operated purely on a percentage-of-the-proceeds payment plan, their incentives would overlap with one another, but not necessarily with plaintiffs. Like the contingent-fee attorney today, both would have some motivation to achieve a higher settlement since it means a greater profit, but the attendant risks of that fee arrangement would plague plaintiffs to an even greater degree. Both financiers and attorneys may prefer to settle quickly (provided the offer exceeds costs and fees), collude with the defendant if the deal financially benefits them, pressure plaintiffs to accept an offer through questionable means, and misallocate settlement funds if it is necessary for achieving the deal's required consensus. So, while a third-party funder could ensure that litigation is not underfunded and might negotiate a reduced attorneys' fee, the savings would benefit the investor, not the plaintiffs.

3. Billable Hours Plus a Small Percentage of the Proceeds

While awarding attorneys a pure percentage of the proceeds would attract creative, entrepreneurial attorneys, the better approach is for the funder to negotiate a billable-hour rate plus a small percentage of the proceeds as a successful litigation bonus.[208] Providing a bonus and having a sophisticated financier oversee the billable

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[206] *See supra* notes 62-73 and accompanying text.

[207] This total range roughly aligns with the percentages permitted in Australia and the United Kingdom. Australian companies receive around 30 percent of the proceeds plus its costs and funders in the United Kingdom receive between 25 and 50 percent of the litigation's proceeds. Martin, *supra* note 128, at 113.

[208] Again, the total amount of the proceeds going to entities other than the plaintiff should not exceed a standard contingent fee rate. This should not run into prohibitions on fee-splitting since the financier is paying the attorney, not splitting the attorneys' fee. When a third party pays someone

hours allays at least some of the traditional objections to having a billable-hour system. These objections include that billable hours encourage lawyers to duplicate their efforts and not communicate effectively with their clients, fail to provide predictable client costs, and penalize efficient and productive lawyers.[209] Having a financier foot the bill actually encourages attorneys to spend time communicating with their clients. And bonuses reward efficiency and productivity while helping to counteract any tendency to unduly prolong the litigation or duplicate effort. Granted, there is still some risk that attorneys might cherry pick certain cases for continued litigation (and the billable hours that accompany them). Yet, the attorney's reputation among the financiers might serve as a failsafe. If the attorney hopes to gain repeat business from financiers while maintaining her reputation as a faithful agent to her clients, then she may only continue to litigate where it best serves her client's interests.

By injecting a sophisticated financier into the lawsuit and making it the largest stakeholder, this arrangement improves the status quo by addressing the two principal problems identified in Part I: the potential funding gap for less established or less solvent plaintiffs' firms and the agency problem that arises when an attorney acts as the lawyer and investor for numerous, disaggregated plaintiffs. First, financiers enable plaintiffs' law firms with less monetary capital to litigate high stakes, resource intensive cases, which increases competition within the private bar.[210] Once a market for funding aggregate litigation emerges, it is also likely to spur competition among financiers, which could, in turn, mean that they would accept a lower percentage of the proceeds for stronger cases.[211]

Second, this proposal incentivizes financiers to monitor the attorneys, while reducing the need for monitoring in the first place. The demand for oversight swelled from bundling financial risk with the attorney's duty of loyalty to clients: self-interest in avoiding financial strain tempted attorneys to engage in self-dealing, overbearing—if not unethical—settlement practices. But uncoupling these divergent pulls permits the financier to negotiate a competitively priced fee and to monitor the monthly costs. With the lawyer's financial wellbeing secured by the financier's nonrecourse investment in the litigation's proceeds, she can faithfully and loyally

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else's fees, it does require informed consent and an assurance that confidential information will remain protected. MODEL RULES OF PROF'L CONDUCT R. 1.8(f), 1.6, 2.1 5.4(c). For a discussion of these issues, see *infra* Part III.D.1.

[209] AMERICAN BAR ASSOCIATION, ABA COMMISSION ON BILLABLE HOURS REPORT 6 (2002).

[210] *See generally* RAND Center for Law & Public Policy, *Conference Proceedings: Third-Party Litigation Funding and Claim Transfer*, *Summary of Remarks by Stephen Yeazell*, at 18 (2010), *available at:* http://www.rand.org/pubs/conf_proceedings/2010/RAND_CF272.pdf ("Third-party funding has the potential to make some smaller firms contenders for large cases, which may, in turn, cause increased competition with larger firms.").

[211] *See* Molot, *supra* note 16, at 107.

represent her clients' best interests as well as counterbalance any undue settlement pressure the financier exerts.

B. Decisionmaking Control

Ethical rules in the United States currently prohibit funders from interfering with or controlling the litigation.[212] And most financiers publicly disavow any authority over the case,[213] though some, like Richard Fields, Juridica's CEO, admit it is "sometimes a challenge to remain hands-off."[214] He explains, "What we do is ask clients to keep us informed if some material event happens in the case, and we ask for quarterly reports. A lot of times we work with clients to set up budgets for the case, and sometimes we bring in people to monitor billing guidelines on the client's behalf."[215] Similarly, Burford Financial observes, "it leaves litigation and settlement decisions to the client and lawyer. It has no authority to influence either. Clients and their lawyers may sometimes choose to solicit Burford's views, but Burford cannot and does not impose its views."[216] The terms of Burford's financing agreement with the Ecuadorian plaintiffs and subsequent reports of Burford's involvement, however, tell a different story: the financing affected settlement decisions by penalizing plaintiffs if they accepted an offer of less than $1 billion, Burford introduced the litigation team to lawyers in the United States, and it reportedly remained "active in case strategy."[217] On the receiving end, lawyers observe that they've "seen everything from funders who want to be involved in everyday management [to] funders who take a hands-off approach."[218]

Introducing a third party into group litigation that already entails fragmented decisionmaking raises questions about the nature and extent of who controls everything from hiring attorneys to consenting to a settlement to pursuing a

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[212] MODEL RULES OF PROF'L CONDUCT R. 1.2(a) (requiring a lawyer to abide by a client's decisions concerning the objectives of representation and to consult with the client as to the means for pursuing those objectives).

[213] *See, e.g.*, Burford Grp. LLC, *supra* note 141, at 5 ("Burford does not replace the party in interest or direct the litigation. Burford does not hire or fire the lawyers, direct strategy or make settlement decisions. Instead, Burford is a purely passive provider of non-recourse financing to a corporate party.").

[214] Maleske, *supra* note 186.

[215] *Id.*

[216] Burford Grp. LLC, *supra* note 141, at 14-15.

[217] Parloff, *supra* note 14; *cf.* Abu-Ghazaleh v. Chaul, 36 So. 3d 691, 693 (Fla. Dist. Ct. App. 2009) (allowing the funder "to approve the filing of the lawsuit; control[] the selection of the plaintiffs' attorneys; recruit[] fact and expert witnesses; receive[], review[], and approve[] counsel's bills; and . . . veto any settlement agreements").

[218] Raymond, *supra* note 128 (quoting James Hosking, who has used third-party funding in international arbitrations).

particular litigation strategy.[219] Were a financier to take on a pure monitoring role, akin to that of an institutional lead plaintiff in securities class actions, it would necessitate more decisional control. In fact, in the United Kingdom, the funders' self-regulatory code allows them to require that litigants request and follow counsel's settlement advice or to seek a second, but binding, opinion from another attorney.[220] But this level of authority reduces what little autonomy plaintiffs' have over their claim once it has been lumped together with others. Aggregating claims empowers lawyers at plaintiffs' expense and makes any meaningful participation in the litigation process obsolete.[221] The need for greater autonomy matters a great deal in claims like personal injury, products liability, and employment discrimination, where claims may be independently economically marketable, but the courts or their attorneys pool them together for efficiency and consistency.[222]

Allocating control to financiers likewise prompts questions about conflicts-of-interests: a financier has fiduciary duties to its investors, whereas attorneys have loyalty obligations to their clients.[223] When financiers are not attorneys, they are not subject to the rules of professional conduct that constrain the attorney-client relationship. This opens an entirely new can of worms: funders could theoretically finance conflicting matters and solicit clients without any corresponding duties of good faith and loyalty.[224]

Fortunately, unbundling financial risk from the attorney's agency requires a less overt monitor. In fact, giving the financier too much authority would simply substitute the contingent-fee lawyer's potentially overbearing settlement demands for the financier's and leave plaintiffs no better off. But the financier must have some say in certain matters. First, like an attorney, a financier decides whether to front the litigation costs for a partial assignment of the plaintiff's proceeds on a case-by-case or litigation-by-litigation basis. Though both the attorney and financier have incentives to vet the case, those incentives differ. A lawyer with only her reputation at stake might represent high-profile social-change litigation, whereas a financier

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[219] *See* Sebok, *supra* note 16, at 111.

[220] CIVIL JUSTICE COUNSEL, A SELF REGULATORY CODE FOR THIRD PARTY FUNDING, 24 para. 7.2 (Dec. 2010), http://blog.internationalpractice.org/wp-content/uploads/2011/07/A-Self-Regulatory-Code-for-Third-Party-Funding.pdf.

[221] *See* Erichson & Zipursky, *supra* note 3, at 269.

[222] Autonomy matters far less when claims are less about compensating the victim and more about deterring the defendant, such as antitrust, consumer fraud, and, for smaller, well-diversified investors, securities fraud cases. If the latter category of cases avoids arbitration, they are still more likely to proceed as class actions or not at all and class actions raise special questions about notice and consent to third party funding that this Article does not address.

[223] As Roger Parloff has pointed out in his article on Burford's financing of the Ecuadorians litigation against Chevron, this complicated relationship has the potential to dilute "the sacrosanct attorney-client relationship." Parloff, *supra* note 14.

[224] Steinitz, *supra* note 145, at 1294.

shouldering the financial risk would prefer cases that promised significant monetary return. Second, the financier negotiates the hourly rate and successful litigation bonus with the plaintiffs' chosen attorney. Though the total amount should not exceed what a plaintiff typically agrees to in a contingent fee, that leaves a sophisticated financier plenty of negotiating room, particularly if it funds numerous plaintiffs.

Finally, even though financiers should not control litigation strategy or dictate the settlement terms, there are two important reasons to let them provide claimants with the equivalent of an advisory opinion. First, if claimants are actually similarly situated and likeminded, then introducing a fresh voice—perhaps one of a very different mind about the settlement offer—injects new information into the discussion, challenges the status quo, and thereby thwarts group polarization and confirmation bias.[225] Introducing cognitively diverse perspectives into group decisionmaking can often lead to novel insights, creative solutions, and enhanced problem solving through robust debate.[226] It likewise helps claimants to avoid premature consensus and reach a more informed decision. Second, it provides transparency—at least to claimants—which promotes accountability and inhibits collusion with attorneys.[227] As critics have pointed out, one of the problems with third-party financiers is that they influence decisionmaking behind the scenes, through the small print of a confidential contract, or by privately conversing with the lawyers. Giving them the opportunity to present their position to the claimants prompts them to go "on the record," so to speak, and provide a reasoned opinion about the settlement's merit. The claimants can then judge for themselves whether that position is contrary to their best interests, seek competent advice from counsel, and then decide whether to settle.[228]

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[225] *See* CASS R. SUNSTEIN, WHY SOCIETIES NEED DISSENT 129-30 (2003); Michael A. Hogg & Sarah C. Hains, *Friendship and Group Identification: A New Look at the Role of Cohesiveness in Groupthink*, 28 EUR. J. SOC. PSYCHOL. 323, 323-35 (1998); Ulrich Klocke, *How to Improve Decision Making in Small Groups: Effects of Dissent and Training Interventions*, 38 SMALL GRP. RES. 437, 437-38, 460-62 (2007).

[226] SCOTT E. PAGE, THE DIFFERENCE: HOW THE POWER OF DIVERSITY CREATES BETTER GROUPS, FIRMS, SCHOOLS, AND SOCIETIES 7-8 (2007); L. Hoffman & N. Maier, *Quality and Acceptance of Problem Solutions by Members of Homogenous and Heterogeneous Groups*, 62 J. ABNORMAL & SOC. PSYCHOL. 401 (1961); Eden B. King et al., *Conflict and Cooperation in Diverse Workgroups*, 65 J. SOC. ISSUES 261, 272 (2009); Elizabeth Mannix & Margaret A. Neale, *What Differences Make a Difference?: The Promise and Reality of Diverse Teams in Organizations*, 6 AM. PSYCHOL. SOC'Y 31, 33-35, 42-43 (2005); C. Nemeth, *Differential Contributions of Majority and Minority Influence*, 93 PSYCHOL. REV. 23 (1986); Stefan Schulz-Hardt et al., *Dissent as a Facilitator: Individual- and Group-Level Effects on Creativity and Performance*, *in* THE PSYCHOLOGY OF CONFLICT MANAGEMENT IN ORGANIZATIONS 149, 150-54 (Carsten K.W. De Dreu & Michele J. Gelfand, eds., 2008).

[227] *See* Issacharoff & Ortiz, *supra* note 8, at 1664.

[228] *But see* ABA Comm'n on Ethics 20/20, *supra* note 146, at 29 (suggesting that the client might be able to delegate settlement authority to a financier).

C. The Litigation-Financing Agreement

Anytime a sophisticated, repeat-player contracts directly with what could be a legally unsophisticated clientele, the potential for overreaching exists. Preventing overreaching demands a mix of informed consent in writing *ex ante* and the ability to fairly resolve disputes *ex post*. First, because the attorney is typically the one who will refer clients to financiers, informed consent obligates that attorney to review the funding agreement on the client's behalf and fully disclose all of the agreement's terms.[229] The attorney should: disclose the extent of her relationship with the funder,[230] discuss the benefits of the funding arrangement (such as the ability to loyally represent the client without the tugs of financial self-interest), explain how the contractual terms could adversely affect the client's interests and the drawbacks that could result from signing it, advise the client about seeking advice from other counsel, and explain that other attorneys might be willing to represent the client on a traditional contingent-fee basis.[231]

Second, in addition to providing informed consent in writing, funding agreements should not interfere with the client's right to terminate the lawyer-client relationship at any time.[232] This not only avoids a conflict with public policy and ethical limitations,[233] it gives the client some immediate recourse if she feels that the attorney is not acting in her best interest.[234] Because discharging an attorney could

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[229] Most states that have considered whether it is appropriate to refer clients to third-party funders have concluded that it is. *See, e.g.*, State Bar of Ariz. Comm. on the Rules of Prof'l Conduct, Ethics Op. 91-22 (1991); D.C. Bar Legal Ethics Comm., Ethics Op. 196 (1989); Md. State Bar Ethics Comm., Advisory Op. 89-15 (1988); Nev. State Bar Standing Comm. on Ethics and Prof'l Responsibility, Formal Op. 29 (2003); N.J. Supreme Court Advisory Comm. on Prof'l Ethics, Advisory Op. 691 (2001); N.Y.C. Bar Ass'n Comm. on Prof'l and Judicial Ethics, Formal Op. 2011-02 (2011).

[230] "[T]he client is entitled to know about the risks presented by the lawyer's financial and other incentives created by the contract, and to have an opportunity to provide or decline informed consent." ABA Comm'n on Ethics 20/20, *supra* note 146, at 19.

[231] *See generally* MODEL RULES OF PROF'L CONDUCT R. 1.0(e) & cmt. 6 (2011) (noting that the lawyer must "[o]rdinarily . . . disclos[e] . . . the facts and circumstances giving rise to the situation," the "material advantages and disadvantages of the proposed course of conduct and a discussion of . . . other . . . options," and that "[i]n some circumstances it may be appropriate for a lawyer to advise a client . . . to seek the advice of other counsel); MODEL RULES OF PROF'L CONDUCT R. 1.4(b); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 20, cmt. f (2011); ABA Comm'n on Ethics 20/20, *supra* note 146, at 19.

[232] *But see* ABA Comm'n on Ethics 20/20, *supra* note 146, at 25 (concluding that giving a financier the authority to discharge an attorney is an enforceable contractual provision absent duress or unconscionability).

[233] *See e.g.,* Balla v. Gambro, Inc., 584 N.E. 2d 104 (Ill. 1991); Mich. State Bar Standing Comm. on Prof'l Ethics, Advisory Op. RI-321 (2000); MODEL RULES OF PROF'L CONDUCT R. 1.16(a)(3), 1.16(c); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS §§ 31-32.

[234] *See* Issacharoff & Ortiz, *supra* note 8, at 1646.

affect the agent's broader reputation among other clients, this also helps prevent wrongful conduct.[235] Third, deterring overreaching and collusion entails the possibility of *ex post* judicial review, a subject explored shortly in Part III.B.2.

Claimants do, however, have an obligation to provide accurate information to both their attorney and financier. Withholding material facts could induce an investor to fund a claim on a fraudulent basis. When that is the case, financiers should be permitted to cease funding the litigation. For example, Juridica recently stopped funding S&T Oil Equipment & Machinery Ltd. in its international arbitration against Romania when King & Spalding withdrew from representing S&T, citing concerns that it failed to produce a critical piece of evidence.[236] In addition to rescinding its funding, Juridica also demanded that S&T reimburse it for litigation expenses since Juridica believed that S&T materially misrepresented the case's prospects of success, failed to disclose material information, and withheld key facts.[237]

D. Implications for Reform

As one might imagine, shifting the status quo from contingent-fee arrangements to litigation-funding agreements necessitates reexamining historical bans on maintenance and champerty as well as contemplating how a financier may affect the attorney-client privilege, work-product doctrine, and attorney confidentiality. This section begins to contemplate those issues while citing more in-depth sources for the interested reader. It likewise considers how financiers might affect horizontal equity among similarly situated plaintiffs in multidistrict litigation and ways to combat free-riding from other plaintiff's attorneys.

1. Augmenting Legal and Ethical Rules

First, if financiers take a more active role in funding aggregate litigation, they need to be able to independently evaluate the claim's merits and communicate with both the plaintiffs and the attorneys without waiving plaintiffs' attorney-client privilege or losing objections based on the work-product doctrine.[238] Although some financiers rely principally on publicly filed pleadings and memoranda and thus do not

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[235] *Id.*

[236] Nate Raymond, *New Suit Against Juridica Exposes Cracks in Litigation Funding Model*, THE AMLAW DAILY, Mar. 15, 2011, http://amlawdaily.typepad.com/amlawdaily/2011/03/litdailyjuridica.html.

[237] Letter from Timothy D. Scrantom, Dir. of Juridica Capital Mgmt. Ltd., to Valerian Simirica, S&T Oil Equip. & Mach. Ltd. (Nov. 10, 2009), *available at* http://amlawdaily.typepad.com/03102011juridica_1109recession.pdf.

[238] *See* MODEL RULES OF PROF'L CONDUCT R. 1.6 (2010) (discussing confidentiality in the client-lawyer relationship); FED. R. EVID. 502.

need privileged information,[239] it seems that a financer considering whether to invest millions of dollars into funding aggregate litigation would need more information. Sharing privileged information requires plaintiffs' informed consent to satisfy attorneys' ethical duties of confidentiality,[240] but it also entails considering the attorney-client privilege and the work-product doctrine. Because lawyers generally waive the work-product doctrine only when they make disclosures that substantially increase the likelihood of putting documents in their adversary's hands,[241] it raises fewer concerns than the attorney-client privilege.

One possibility for addressing the attorney-client privilege is to extend the common-interest doctrine to include financiers who invest in the lawsuit as well as those who considered investing.[242] Covering the latter category of investors encourages price competition among financiers without jeopardizing plaintiffs' confidential information. The common-interest doctrine evolved from situations where two clients retained the same attorney to pursue their common interest and has long been used by insurance companies, in joint defense strategies (such as by asbestos and tobacco defendants), and by plaintiffs involved in group litigation.[243] In these contexts, the doctrine extends to "two or more clients with a common interest in a litigated or nonlitigated matter" who are represented by the same or separate lawyers to encourage full and efficient case preparation.[244] Although the third-party

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[239] ABA Comm'n on Ethics 20/20, *supra* note 146, at 33.

[240] MODEL RULES OF PROF'L CONDUCT R. 1.6(a) (permitting a client to give informed consent to disclose confidential information).

[241] Mondis Tech. v. LG Elecs., Nos. 2:07-CV-565-TJW-CE, 2:08-CV-478-TJW, 2011 WL 1714304 (E.D. Tex. May 4, 2011) (finding that a party could share information containing work-product information with investors without waiving its protections).

[242] Currently, substantial uncertainty surrounds the privilege issue. *See* FED. R. EVID. 502(b) (noting that inadvertent disclosure may waive the privilege); Leader Techs. v. Facebook, Inc., 719 F. Supp. 2d 373 (D. Del. 2010) (refusing to extend the common-interest exception to include a financier); State Bar of Ariz. Comm. on the Rules of Prof'l Conduct, Ethics Op. 01-07 (2001); Fla. Bar Comm. on Prof'l Ethics, Op. 00-3 (2002); State Bar of Mich. Standing Comm. on Prof'l and Judicial Ethics, RI-321 (2000); N.J. Advisory Comm. on Prof'l Ethics, Op. 691 (2001); Supreme Court of Tex. Prof'l Ethics Comm., Op. 558 (2005).

[243] *E.g.*, Reavis v. Metro. Prop. & Liab. Ins. Co., 117 F.R.D. 160, 165 (S.D. Cal. 1987); *see also* CHRISTOPHER B. MUELLER & LAIRD C. KIRKPATRICK, EVIDENCE §§ 5.14, 5.15 (3d ed. 2003); EDNA SELAN EPSTEIN, THE ATTORNEY-CLIENT PRIVILEGE AND THE WORK-PRODUCT DOCTRINE 274-75 (5th ed. 2007); James M. Fischer, *The Attorney-Client Privilege Meets the Common Interest Arrangement: Protecting Confidences While Exchanging Information for Mutual Gain*, 16 REV. LITIG. 631, 632 (1997).

[244] RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 75 (2000) (applying the common-interest privilege to those with the same attorney); RESTATEMENT (THIRD) OF THE LAW GOVERNING LAWYERS § 76 (2000) (applying the common-interest privilege to those with separate attorneys); *see also* CHRISTOPHER B. MUELLER & LAIRD C. KIRKPATRICK, EVIDENCE §§ 5.14, 5.15 (3d ed. 2003). There have been arguments that the common interest privilege only applies to legal interests in potential or ongoing litigation, but this potential limit should not pose a problem in the third-party financing context. *See, e.g.*, United States v. Duke Energy Corp., 214 F.R.D. 383, 390

financier seems to fit neatly under this common-interest umbrella, there is one critical matter worth clarifying: the financier and the plaintiff cannot be considered joint clients of the plaintiff's attorney. If that were the case, the lawyers would have duties of loyalty to the financier, not just her client. That would undermine the disaggregated incentive structure that promotes loyalty to plaintiffs.

Second, states should continue to lift the historical prohibition on champerty such that the enforceability of a financing agreement does not hinge on a particular state's laws or an ad-hoc balancing approach to conflict of laws, both of which provide further impetus for forum shopping. One recent survey showed that twenty-six of fifty-one jurisdictions (including the District of Columbia) permit champerty to some degree so long as the financier does not promote clearly frivolous litigation, participate in "malice champerty" ("meritorious litigation employed for an improper end"),[245] or "intermeddling" (controlling trial strategy or settlement).[246] Further, as Anthony Sebok has argued in detail, the arguments against assignment and maintenance are "not currently persuasive from either a historical or jurisprudential perspective."[247] And most studies about champerty predict that lifting this ban will be beneficial by increasing access to justice and improving the likelihood that settlements will reflect the claim's merit as opposed to economic pressures.[248]

Questionable enforceability has driven commercial-dispute lenders to include arbitration provisions within their funding agreements, many of which require

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(M.D.N.C. 2003) (requiring all interested parties to share a common legal interest related to ongoing or potential litigation).

[245] Sebok, *supra* note 16, at 104-05.

[246] ABA Comm'n on Ethics 20/20, *supra* note 146, at 12; Paul Bond, *Making Champerty Work: An Invitation to State Action*, 150 U. PA. L. REV. 1297 app. at 1333-41 (2002); Sebok, *supra* note 16, at 98-99 n.162, 104-05 (listing jurisdictions that permit some degree of champerty as Arizona, California, Colorado, Connecticut, Florida, Hawaii, Iowa, Kansas, Maine, Maryland, Massachusetts, Michigan, Montana, New Hampshire, New Jersey, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, South Carolina, Tennessee, Texas, Washington, and West Virginia) (later data suggests that Missouri should not be included among these states).

[247] Sebok, *supra* note 16, at 133.

[248] Peter Charles Choharis, *A Comprehensive Market Strategy for Tort Reform*, 12 YALE J. ON REG. 435, 473 (1995); Jonathan T. Molot, *A Market in Litigation Risk*, 76 U. CHI. L. REV. 367 (2000); Jonathan T. Molot, *A Market Approach to Litigation Accuracy* (10th Annual Legal Reform Summit, U.S. Chamber Inst. for Legal Reform, Oct. 28, 2009). Some commentators have argued that lifting champerty bans will encourage frivolous lawsuits because once financiers exhaust their cache of meritorious cases, they will turn to frivolous ones. *See, e.g.*, Paul H. Rubin, *Third Party Financing of Litigation* (Third Party Financing of Litigation Roundtable, Searle Ctr., Nw. Univ. Law Sch. Sept. 24-25, 2009), *available at* http://www.law.northwestern.edu/jep/symposia/JEP_CJ_2009_Rubin.pdf. This argument, however, is unlikely in aggregate litigation, where strict claims administration procedures post-settlement help weed out (or pay less to) weak claims.

international arbitration,[249] and none of which help develop the law surrounding alternative litigation financing. This move toward international arbitration, particularly in jurisdictions like the United Kingdom, is somewhat understandable given the uncertainty of domestic champerty and maintenance laws and the United Kingdom's general acceptance of alternative financing. If funding agreements simply included forum-selection clauses, some courts would refuse to dismiss or transfer those cases to the specified forum if doing so would contravene that state's public policy.[250]

But international arbitration requirements do little for one-time plaintiffs. Although commercial disputes involve a sophisticated clientele who may be familiar with the ins and outs of international arbitration, requiring the average mass-tort or employment-discrimination victim to arbitrate her dispute internationally would be prohibitively expensive and inconvenient; she would be forced to forgo her grievance, regardless of its merit. Plus, if foreign countries take alternative legal and ethical approaches to conflicts of interest, they could raise questions about impropriety that undermine both the funding agreement and the arbitration's legitimacy.[251]

2. Tailoring Judicial and Ethical Checks

Both the potential for overreaching in the litigation-funding agreement and the potential collusion between attorneys and financiers pose critical concerns. Although these concerns are interrelated pragmatically—an attorney who colludes

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[249] *See, e.g.*, Treca Financial Solutions and Claimants Funding Agreement, at 27 para. 23.2, *available at* http://theamazonpost.com/wp-content/uploads/Mastro-declaration-Exs-1-10-05jul11.pdf (funding agreement between Buford Financial and the Ecuadorian plaintiffs in their litigation against Chevron) ("Any dispute, controversy or claim arising out of or connection with this Agreement, including any question regarding its formation, existence, validity, interpretation, performance, breach or termination and including any dispute about the value of the Award, shall (to the exclusion of any other forum) be referred to and finally resolved by arbitration administered by the International Centre for Dispute Resolution in accordance with its International Arbitration Rules . . . ."); Complaint at para. 28, S&T Oil Equip. & Mach., Ltd v. Juridica Inv. Ltd., No. H-11-542 (S.D. Tex. Feb. 14, 2011), *available at* http://amlawdaily.typepad.com/03102010juridica_complaint.pdf (alleging that Juridica "fraudulently induced plaintiffs into entering into the arbitration provision included in the Investment Agreement, which provided for arbitration in the Bailiwick of Guernsey under London Court of Arbitration (LCIA)").

[250] *See generally* M/S Bremen v. Zapata Off-Shore Co., 407 U.S. 1, 16-17 (1972) (suggesting that forum-selection clauses that contravene an important public policy of the forum might be unenforceable).

[251] Complaint at para. 28, S&T Oil Equip. & Mach., Ltd v. Juridica Inv. Ltd., No. H-11-542 (S.D. Tex. Feb. 14, 2011), *available at* http://amlawdaily.typepad.com/03102010juridica_complaint.pdf (alleging that Juridica "failed to disclose that at least one of [its] non-executive directors and another lawyer, Daniel Brennan, is and was at the time of the arbitration agreement's execution, a member of the LCIA board of directors").

with the financier is likely to encourage clients to sign unconscionable funding agreements—widespread use of arbitration provisions make it nearly impossible to review these issues outside of legal ethics proceedings. The problems are both practical and legal. First, the practical: arbitrations—particularly those with international venues—and the likely need to retain alternative counsel make it extraordinarily difficult for all but the wealthiest plaintiffs to pursue their rights against investors or for courts to develop the laws surrounding alternative litigation financing.[252] Second, the legal: *AT&T Mobility v. Concepcion* means that financiers can prevent class or group arbitration even if they financed plaintiffs en masse.[253] Freedom of contract and courts' deference to arbitration provisions under the Federal Arbitration Act further limit judicial solutions.[254] Even though a plaintiff might claim that the funding agreement is unenforceable based on contractual defenses like fraud, duress, or unconscionability, unless she specifically challenges the arbitration provision, courts may send those questions to the arbitrator to decide.[255]

Market solutions have limited potential to do what judicial remedies cannot. If financiers compete for the best cases (meritorious claims represented by attorneys with solid reputations), then the informed consumer can shop around for financing without arbitration strings attached. The trouble is, attorneys are likely the ones referring clients to a financier. And attorneys' preferred financiers may depend more

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[252] Most studies of disciplinary actions for excessive fees or attorney misconduct support this notion. *See* ABA COMM'N ON EVALUATION OF DISCIPLINARY ENFORCEMENT, LAWYER REGULATION FOR A NEW CENTURY 11 (1992) ("The disciplinary system was not designed to address complaints about the quality of lawyers' services or fee disputes."); Lester Brickman, *Contingency Fee Abuses, Ethical Mandates, and the Disciplinary System: The Case Against Case-by-Case Enforcement*, 53 WASH. & LEE L. REV. 1339, 1345 (1996) (noting that contingency fee lawyers are "virtually never disciplined for charging unreasonable fees"). *But see* Christopher R. Drahozal, *Arbitration Costs and Contingent Fee Contracts*, 59 VAND. L. REV. 729, 734 (2006) (arguing—ironically in the context of this Article—that contingent fees can provide "a mechanism by which arbitration can enhance, rather than restrict claimants' access to justice").

[253] 131 S. Ct. 1740 (2011); Jessie Kokrda Kamens & Tom P. Taylor, *Will Class Actions Survive Ruling By Supreme Court in* Concepcion*?*, BNA CLASS ACTION LIT. RPT., May 13, 2011.

[254] *See* Thomas V. Burch, *Regulating Mandatory Arbitration*, UTAH L. REV. (forthcoming 2012), *available at* http://ssrn.com/abstract=1793303.

[255] *See* Buckeye Check Cashing, Inc. v. Cardegna, 546 U.S. 440, 444-46, 448-49 (2006) (holding that challenges to the validity of the agreement to arbitrate may be litigated in court, whereas challenges to the contract as a whole must be litigated before the arbitrator); Prima Paint Corp. v. Flood & Conklin Mfg. Co., 388 U.S. 395, 404 (1967) ("[I]n passing upon a § 3 application for a stay while the parties arbitrate, a federal court may consider only issues relating to the making and performance of the agreement to arbitrate."); Nagrampa v. MailCoups, Inc., 469 F.3d 1257, 1271 (9th Cir. 2006); Toledano v. O'Connor, 501 F. Supp. 2d 127, 140 (D.D.C. 2007) ("The district court is therefore the appropriate forum for adjudicating all of plaintiffs' challenges—to the arbitration provision, to enforcement of that provision, and to the existence of the contract containing that provision.").

on the hourly rate and percentage of the proceeds the financier will pay them than the clients' best interests. This brings us back to the potential for collusion between the financier and attorney. Unlike clients, who are typically one-shot players, financiers and lawyers are both repeat players; their relationship is more enduring.[256]

This potentially powerful bond between financiers and attorneys suggests that judges must play a mitigating role. But two things must happen before they can do so. First, they must know that an alternative-financing arrangement exists.[257] Accordingly, in multidistrict litigation, there should be mandatory, in camera disclosure of financing agreements. Currently, financing agreements contain confidentiality provisions and financiers regularly require plaintiffs to sign additional non-disclosure agreements.[258] Although these measures keep the defendant from exploiting this information, submitting the funding agreement to the judge in camera allows the judge to not only learn of its existence and ensure its terms are not unconscionable,[259] but to recuse herself if she has a disqualifying relationship with the financier.[260] Moreover, should it become necessary, this enables the judge to report unethical behavior between attorneys and financiers to the relevant bar authorities.

Second, as Congress has done in similar areas of consumer concern,[261] it, or perhaps the newly minted Bureau for Consumer Financial Protection, should

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[256] Steinitz, *supra* note 145, at 1325.

[257] This is somewhat akin to Rule 7.1, which requires corporations to identify any parent corporation owning more than 10% of a party's stock. FED. R. CIV. P. 7.1.

[258] *See, e.g.*, Complaint at para. 28, S&T Oil Equip. & Mach., Ltd v. Juridica Inv. Ltd., No. H-11-542 (S.D. Tex. Feb. 14, 2011); Treca Financial Solutions and Claimants Funding Agreement, *supra* note 249, at 18 para. 12 (requiring claimants not to disclose the terms of the agreement for seven years after its termination and to "destroy or return all Funder information to the Funder").

[259] Judges may ensure that fees adhere to ethics and professional responsibility standards even absent a fee challenge. Rosquist v. Soo Line R.R., 692 F.2d 1107, 1111 (7th Cir. 1982); Jacobs v. Mancuso, 825 F.2d 559, 564 (1st Cir. 1987); *In re* Zyprexa Prods. Liab. Litig., 424 F. Supp. 2d 488 (E.D.N.Y. 2006); Farmington Dowel Prod. Co. v. Forster Mfg. Co., 297 F. Supp. 924, 925-30 (D. Me. 1969); Charles Kocoras, Comment, *Contingent Fees—A Judge's Perch*, 47 DEPAUL L. REV. 421, 422 (1998).

[260] *See, e.g.*, Parloff, *supra* note 14 (discussing an instance in which a special master learned that he was co-counsel with a member of the hedge fund's board).

[261] *See, e.g.*, John Warner National Defense Authorization Act for Fiscal Year 2007, Pub. L. No. 109–364, 120 Stat. 2083 (2006) (exempting military personnel from having to arbitrate consumer-credit disputes); Food, Conservation, and Energy Act of 2008, Pub. L. No. 110–234, § 210, 122 Stat. 923 (2008) (permitting parties to opt out of arbitration in livestock and poultry contracts); Department of Defense Appropriations Act of 2010, Pub. L. No. 111-118, § 8116, 123 Stat. 3409 (2009) (prohibiting the government from hiring employers that require their employees to arbitrate Title VII claims or sexual assault or harassment claims); Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010) (creating the Consumer Protection Financial Bureau and giving that Bureau power over arbitration provisions in "consumer financial products and services" agreements); Motor Vehicle Franchise Contract Arbitration Fairness

prohibit arbitration in consumer-financing agreements.[262] This would ensure some transparency in the funding process through enforcement challenges, allow consumers to vindicate their contractual rights in a convenient forum, and, through judicial adjudication, outline the permissible bounds of litigation-funding agreements. Potential judicial enforcement also deters collusive behavior between the financier and the plaintiffs' attorneys; when the two know that the agreement is not shrouded in arbitration's confidentiality and could land before a judge (and in publicly filed documents), they are far less likely to engage in clandestine behavior.

3. Maintaining Horizontal Equity Among Plaintiffs

Just as they do now, well-financed, well-established law firms are likely to eschew alternative financing.[263] Being paid on an hourly basis plus a small percentage of the proceeds may not generate the same extravagant fees that a traditional contingent fee might. That plus having to answer to an intermediary may only fuel the potential for horizontal inequity among similarly situated plaintiffs. For example, in the ground zero litigation, Napoli Bern tried to pass the interest costs of borrowing money on to its clients, whereas another firm representing around 690 clients borrowed nothing, meaning that the latter plaintiffs would have received more money for similar claims.[264] For plaintiffs, this means a two-track system where those with similarly situated claims may receive less money depending on how their lawyer financed the litigation. To minimize the danger of disparate fees, the system I have proposed employs current contingent-fee rates as a presumptively adequate ceiling for financiers to include in their agreements. This keeps the

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Act of 2001, S. 1140, 107th Cong. (2001) (prohibiting motor-vehicle manufacturers, importers, and distributors from requiring arbitration in franchise agreements); *see also* Burch, *supra* note 254; Steven Greenhouse, *Labor Board Supports Class Action for Workers*, N.Y. TIMES, Jan. 7, 2012, at B1.

[262] Though Congress has ample authority for prohibiting arbitration awards, the Bureau's authority is less certain. Dodd-Frank gives the Bureau the authority to "regulate the offering of . . . consumer financial products . . . under Federal consumer financial laws" and to regulate and restrict mandatory pre-dispute arbitration agreements. Dodd-Frank Act § 1011. Dodd-Frank defines "consumer financial product" as extending credit to consumers "primarily for personal, family, or household purposes." *Id.* § 1012. Although funding agreements enable consumers to litigate in hopes of receiving damages that compensate them, their family, or their household, it is unclear whether it will decide this falls within its auspices (after all, to date Congress hasn't appointed anyone to lead the Bureau). Suzanna Andrews, *The Woman Who Knew Too Much*, VANITY FAIR, Nov. 2011, at 184; Ben Protess, *Nominee to Lead Consumer Agency Clears a Hurdle*, N.Y. TIMES, Oct. 6, 2011, http://dealbook.nytimes.com/2011/10/06/cordray-nomination-advances.

[263] Frankel, *supra* note 133 ("Well-financed plaintiffs firms tend to stay away from litigation finance companies; as Christopher Seeger of New York's Seeger Weiss notes, 'It's ridiculous how much they charge.' Firms that can afford to usually prefer to invest their own capital in experts, case screening, discovery and trial expenses.").

[264] Goldstein & Edelman, *supra* note 14.

absolute percentage of the proceeds going to entities other than the plaintiff similar across-the-board.

4. Taxing Free-riders

Having attorneys with different funding arrangements involved in the same multidistrict litigation exacerbates a concern about free riders when some attorneys perform common-benefit work for all plaintiffs. The concern exists regardless of whether financiers are involved,[265] but the way in which judges have handled compensation in the past—by adding to and subtracting from fee awards—would not only interfere with funders' contractual rights, it could deter them from investing in aggregate litigation.

If the established plaintiffs' firms self-fund and continue to use their strong reputations to leverage favorable settlements from defendants, they are likely to be the chosen ones serving on plaintiffs' steering committees and performing common-benefit work. Traditionally, judges have used the common-fund theory to reduce the fees of lawyers on the litigation's outskirts who may have large client inventories, but have done little to advance the litigation—whether by choice or not.[266] But this traditional system creates free riders once financiers enter the picture. Attorneys paid on a "billable-hour-plus" basis would still receive less—they're doing less work—but the financiers could receive more than they bargained for due, in part, to other attorneys' efforts. Conversely, if the billable-hour attorney performed common-benefit work, she might receive less remuneration than would counsel working on a contingent-fee arrangement. Yet, her work benefits all of the plaintiffs. So, unless the same investor had a funding relationship with each plaintiff, the other plaintiffs' attorneys would be enriched without cost.

Both situations suggest that something other than the status quo is appropriate, but judicial interference with the funding relationship could undermine the positive effects of unbundling agency and risk. Solving this problem entails reconsidering how judges compensate plaintiffs' steering committees and common-benefit counsel. As Professors Silver and Miller have argued, compensation is best addressed by taxing the total recovery from the multidistrict litigation and then subtracting that tax

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[265] Curtis & Resnik, *supra* note 59, at 444 ("The worry is about 'free riders' who obtain clients and receive, by private contract, significant percentages of the clients' recoveries for minimal work.").

[266] *Id.* at 430, 434 ("Aggregation inspires superintendence of fees for a range of reasons. Firs, the work of judges on attorneys' fees in all kinds of cases has exposed the courts to billing practices that upset them; judges have become impatient and distressed at the size of bills and the relationships between outcomes and costs."). As Professors Silver and Miller explain, when judges appoint attorneys to inside positions, they "create[] relationships of dependency" such that attorneys on the outskirts must "rely on a coterie of litigation managers to develop their clients' cases. They disabled lawyers clients also lost control. They were at the mercy of the lawyers they never hired and could not discharge." Silver & Miller, *supra* note 57, at 119.

from each client's attorney's fee (or financier's proceeds) such that the tax is spread across all participating plaintiffs in proportion to their recovery.[267] Although this means that financiers must consider the tax in drafting the litigation-funding agreement and subtract it from their overall proceeds, this is a relatively straightforward fix.

IV. COSTS, BENEFITS, AND OBJECTIONS

This Article has set forth, in broad-brush strokes, the normative argument in favor of allowing third-party funders to serve as the missing monitor in aggregate litigation. By unbundling an attorney's duty as an agent from that of a financier we can alleviate a principal incentive to engage in unethical behavior and, by allowing financiers to invest in aggregate litigation's outcome, create a intermediary monitor. But though this manages some of the principal-agent problems in nonclass aggregation, it introduces a new twist, another entity, and a unique set of incentives that could work to the plaintiffs' detriment. So, does this improve the status quo?

This final Part addresses that question by summarizing this proposal's benefits as well confronting lingering concerns that are likely to arise if third parties assume a monitoring function. Many of the primary benefits have been discussed already, such as (1) unbundling the lawyer's financial risk from her duty of loyalty; (2) enabling the financier to negotiate a competitive rate, monitor the monthly bills, state its position on settlement, and thereby stymie group polarization; (3) engendering a system of checks where a loyal attorney counterbalances a financier's push for settlement; (4) using billable hours to motivate attorneys to counsel clients through litigation decisions, and (5) avoiding ethically questionable practices like quick settlements.

To these benefits, add the following four advantages. First, like well-capitalized contingent-fee attorneys, third-party financiers may pursue nonclass aggregation that would be uneconomical as a stand-alone case, but provides a significant return in the aggregate. This does not include small-stakes or negative-value claims, such as consumer-fraud cases, because individual plaintiffs are unlikely to come forward in numbers that make litigation viable. It would, however, include claims like those pursued by the women in *Dukes*, whose individual claims might not make it economical to take on a corporation like Wal-Mart, but are worth litigating collectively. Without this kind of socially desirable deterrence-based litigation,

[267] *Id.* at 161. One of the principal objections to this approach is that attorneys may aggregate low-value cases in hopes of achieving judicial appointment; the authors suggest that judges could readily identify and exclude weak cases through, for example, requiring a licensed medical doctor to certify that the plaintiff has the particular disorder in question. *Id.* at 163-64.

corporations could easily trample employee or consumer rights that are otherwise uneconomical to pursue.[268]

Second, outside funding increases competition among the plaintiffs' bar in that it allows smaller or less-established firms to litigate cases they might not otherwise be able to afford.[269] Competition could foster innovation and creativity and drive down transaction costs for plaintiffs. And because financiers want well-credentialed attorneys handling the cases they fund, their vetting process helps screen unqualified attorneys.

Third, financiers may improve the correlation between settlement value and the case's merits.[270] When one-time, risk-averse plaintiffs follow their attorney's advice and that advice is animated by attorney self-interest or collusion with the defendant, the settlement value does not reflect the lawsuit's merits. Permitting a financier to assume the financial risks diminishes this possibility; attorneys can genuinely advise clients about the costs and benefits of proceeding and make realistic settlement demands. Finally, as repeat players, financiers are likely to be more efficient at monitoring litigation costs and keeping attorneys' fees manageable than one-time clients.[271]

These benefits do not come without costs. Absent a judge's ability to assess the financing agreement's fairness and a claimant's capacity to air allegations of collusion between the financier and attorney in a judicial—as opposed to arbitral—forum, the potential for overreaching exists. And while alternative financing may frequently alleviate the access-to-justice problem by shifting the risk of loss to the financier, it also further commodifies legal claims. Of course, contingent-fee plaintiffs' attorneys have long been monetizing claims, often regardless of their clients' stated aims, which suggests that the status quo may not be all that different with third-party financing.[272] Either way, law firms have few incentives to take cases like employment-discrimination and civil-rights claims, where injunctive and declaratory relief is a nontrivial component. One recent empirical study showed that 75 percent of civil-rights, 29 percent of labor-and-employment, 37 percent of consumer, and 34 percent of employee-benefits class settlements included some injunctive or declaratory relief.[273] While fee-shifting statutes help by shifting litigation costs to the

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[268] *See* Hylton, *supra* note 16, at 27; Schanzenbach & Dana, *supra* note 177, at 12.

[269] Frankel, *supra* note 133 ("Well-financed plaintiffs firms tend to stay away from litigation finance companies; as Christopher Seeger of New York's Seeger Weiss notes, 'It's ridiculous how much they charge.' Firms that can afford to usually prefer to invest their own capital in experts, case screening, discovery and trial expenses.")

[270] *See* Molot, *supra* note 16, at 101.

[271] *See* Hylton, *supra* note 16, at at 27.

[272] *See* Relis, *supra* note 150, at 721.

[273] Fitzpatrick, *supra* note 63, at 824 tbl. 3 (studying class-action settlements from 2006-2007). Injunctive or declaratory relief included "modification of terms of employee benefit plans,

defendant, these statutes award fees to a prevailing plaintiff at the end of the lawsuit. This does nothing to alleviate concerns about the increased costs of initiating aggregate litigation, such as higher administrative costs.

This commodification conundrum creates two potential, interrelated problems: *underenforcement* of social-change and public-interest litigation and *inaccessibility of indivisible remedies*. Public-interest and social-change litigation have no hard-edged definitions, but include claims like race and sex discrimination in the workplace, sexual harassment, Fair Debt Collection Practices Act violations, housing desegregation or discrimination suits, American with Disabilities Act violations, and even toxic torts requiring environmental cleanup. Each of these claims includes a hybrid of divisible and indivisible relief. Take Title VII, for example. Were funders to invest in Title VII litigation for a percentage of the plaintiffs' recovery, they would care more about compensatory damages, punitive damages, and backpay—not injunctive or declaratory relief, even though Congress first enacted Title VII with those social-change goals in mind.[274]

Still, the availability of compensatory and punitive damages might spur funders to bankroll aggregated cases that might otherwise be ignored. Financiers would invest for the profit, but since attorneys must bring all available claims on behalf of their clients and pursue their clients' wishes, they would request injunctive or declaratory relief, too. And because clients retain control over settlement decisions, there is less danger that attorneys might trade meaningful reforms for compensation, at least assuming that's what their clients want. Moreover, private attorneys' efforts in this regard might then enable governmental agencies to ride their coattails and bring separate suits for injunctive relief.

Another option would be for judges to allow financiers to receive a percentage of the group's recovery under the fee-shifting statutes just as they would an attorney. If indivisible relief is a major remedial component, then courts could still use the fee-shifting statute to determine a base amount and then factor in a higher multiplier based on the litigation's "undesirability" and the results obtained.[275] Alternatively, if

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modification of compensation practices, changes in business practices, capital improvements, research, and unliquidated repairs to property." *Id.*

[274] *See generally* THE RIGHT HONOURABLE LORD JUSTICE JACKSON, REVIEW OF CIVIL LITIGATION COSTS: FINAL REPORT 118 (2009), *available at* http://www.judiciary.gov.uk/NR/rdonlyres/8EB9F3F3-9C4A-4139-8A93-56F09672EB6A/0/jacksonfinalreport140110.pdf ("Third party funding is not usually feasible where non-monetary relief, such as an injunction or declaration, is the main remedy sought.").

[275] Courts typically consider some or all of the following factors when determining a lodestar amount: (1) the time and labor involved; (2) the novelty and difficulty of the questions; (3) the skill required; (4) preclusion of other employment by the attorney; (5) the customary fee; (6) whether the fee is fixed or contingent; (7) time limitations imposed by the client or by circumstance; (8) the amount involved and the results obtained; (9) the experience, reputation, and ability of the attorneys;

funders loaned money directly to law firms, as Counsel Financial did in funding Napoli Bern's ground zero workers' claims, then courts might consider whether it is appropriate to pass interest charges on to the defendant as part of a fee-shifting regime.[276] In this way, judges can fulfill the legislative intent behind fee-shifting statutes and ensure that social-change litigation and remedies seeking accountability through declaratory and injunctive relief are not a casualty to third-party financing.

CONCLUSION

Alternative litigation financing, if properly engineered, could help alleviate the financial pressure on the attorney-client relationship and thereby encourage ethical behavior in litigating and settling aggregate litigation. Presently, attorneys who specialize in large-scale litigation bear the crushing burden of funding it, a practice that prevents lawyers with less capital from entering the field and tempts those who do to prefer their own financial self-interest over their clients' best interests. If financial risk is no longer an integral part of an attorney's relationship with her clients, it opens the door to several new possibilities. First, financiers might bankroll talented attorneys who could not otherwise afford to initiate aggregate litigation. Second, new entrants could intensify competition among the plaintiffs' bar that could encourage innovation and drive down fees. Finally, given the increased costs and risks associated with multidistrict litigation as opposed to class actions, allowing financiers to enter the picture ensures that meritorious suits will not wither alongside the class action. To be sure, adding an intermediary can introduce competing incentives and is thus not a cure-all for principal-agent problems. Rather, third-party financiers offer one means for managing some of these problems in aggregate litigation.

(10) the "undesirability" of the case; (11) the nature and length of the lawyer-client relationship; (12) awards in similar cases. *See, e.g.*, Johnson v. Ga. Hwy. Express Inc., 488 F.2d 714, 717-19 (5th Cir. 1974).

[276] Judge Hellerstein forbade attorneys from passing the litigation financing's interest cost on to their clients in the ground zero workers litigation. Mireya Navarro, *Judge Rejects $6.1 Million in 9/11 Case Legal Fees*, N.Y. TIMES, Aug. 27, 2010. Given that he cited fairness grounds, this may not be a barrier in fee-shifting litigation since the idea behind fee-shifting statutes is that plaintiffs would not have to incur attorneys' fees at all but for the defendant's wrongdoing.