CHICAGO LAWYER

Getting the best of both worlds : Third-party litigation funding while protecting confidentiality

March 01, 2015

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Imagine the following scenario:

Your longtime client, a privately held company with $500 million in annual revenue, approaches you wanting to file a patent-infringement suit enforcing its rights in its top-selling product against a global conglomerate with several billion dollars in assets.

Your client's general counsel asks you to consider a contingent arrangement, but you cannot work out the finances to everyone's liking. Then, the general counsel asks your advice about obtaining financial support from a litigation funding firm that promises to fund a client's litigation expenses in exchange for a percentage of any recovery.

It sounds like a workable arrangement.

But before the lender agrees to a deal, it wants access to a surprising amount of confidential information — including your firm's assessment of the client's case. You suddenly get a gnawing feeling in the pit your stomach because you are rightly concerned about waiving the privilege, while at the same time wanting to help the client find a solution to the problem.

This scenario is playing out more frequently as the cost of commercial litigation continues to spiral upwards and companies with shrinking budgets find themselves at a disadvantage when looking to file lawsuits to protect their interests.

These lenders may see the courtroom as an arena where the game, so to speak, can only be played by the big boys with deep pockets. This has resulted in the growth of third-party litigation financing firms.

Third-party litigation funders — or alternative litigation financing (ALF) — provide businesses cash advances to fund commercial litigation against more well-funded adversaries.

These firms, often backed by multimillion-dollar private equity portfolios, issue non-recourse loans secured by a stake in the litigation. More businesses consider ALF as an attractive option to pursue cases that might otherwise be cost-prohibitive. However, there lay ethical traps for lawyers representing commercial plaintiffs employing ALF. Chief among those concerns is ensuring that any information provided to an ALF does not waive the privilege.

An ALF entity, like most lenders, does not issue loans without conducting extensive due diligence. Before deciding whether to finance litigation, ALF entities require plaintiffs adhere to broad demands, including providing otherwise privileged and confidential material to assess the merits, potential pitfalls and possibilities for recovery of the proposed litigation.

ALF entities also typically require comprehensive updates as the litigation progresses. Sharing this type of information raises potential ethical considerations implicating the attorney-client privilege and work product doctrine.

Lawyers have the duty to protect and not disclose privileged and confidential client communications. Disclosing privileged information to an ALF entity waives the privilege. Some have tried to apply the common-interest doctrine to avoid waiver.

Most courts, however, reject that approach because the common-interest doctrine only applies when parties share a common legal interest — not a common commercial interest — in the outcome of a case.

The work-product doctrine, on the other hand, provides an effective way to protect disclosure of confidential information to an ALF entity. This is especially true if a non-disclosure agreement is in place between the ALF and the plaintiff.

Unlike the attorney-client privilege, disclosure of work product to a third-party does not automatically waive the privilege. In contrast to the attorney-client privilege, the party asserting waiver has the burden to show that a waiver occurred.

The opposing party must show that a substantial need exists for it to obtain work product and that it faces undue hardship if unable to obtain it. Underlying facts are discoverable, therefore it is unlikely that merely disclosing work product to a third-party constitutes waiver.

An opposing party would have a difficult time establishing a substantial need to obtain a lawyer's thoughts and impressions when it could merely root out the source information.

That said, it is possible that documents prepared for the purpose of securing the financing, as opposed to documents prepared for litigation, are not work product. So there is a risk that those documents may be discoverable.

The next time you face this issue, consider the following advice:

•Request your client provide you written, informed consent before disclosing any privileged or confidential information. Be sure to explain the potential for waiving the privilege and the possible consequences on the outcome of the case, related litigation and future business strategies.

•Advise your client to execute a non-disclosure agreement with the ALF to keep all submitted material confidential. However, even a confidentiality agreement may not prevent waiving the attorney-client privilege to the extent such information is disclosed.

•Advise your client to limit information provided to the ALF to analyses and documents created for the purpose of preparing for litigation so it falls within the work product protections.