What You Should Know About Private Litigation Funding In Patent Disputes

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I. INTRODUCTION

The emergence and expansion of litigation finance has been recognized as one the most significant modern developments in civil litigation. Today, litigation finance is widely used to fund commercial cases, including intellectual property disputes. As market forces and rising litigation costs continue to propel the industry into the mainstream of the United States civil justice system, the fundamentals and ethical implications of litigation finance must be understood by litigators and clients alike.

II. FUNDAMENTALS OF LITIGATION FINANCE

A. What is Litigation Finance?

Litigation finance is any transaction in which a litigation or arbitration claim is used to secure financing from an outside party. In a litigation finance transaction, the financing party provides capital to the claimant in exchange for an interest in the outcome of the case. Financing is provided on a non-recourse basis; as such, the funder that finances the claim only receives a return if the case is successfully settled or results in a collected judgment.

Generally, a litigation funder takes a security interest in the proceeds if the claim is successfully litigated. In such case, the funder receives its investment and a negotiated return with the balance distributed to the claimant. In some rare instances, funders may take security in other litigation-related assets, such as a patent in intellectual property litigation or a claimant's business proceeds.

B. History of Litigation Finance

Litigation finance began in Australia around 2001. At that time, contingency arrangements were not allowed in Australia. Moreover, it was a "loser pays" jurisdiction in which any party that was unsuccessful in court was responsible for the other party's legal costs. Because these costs presented a high financial threshold for bringing a lawsuit, meritorious claims often were not litigated.

A group of Australian insolvency practitioners saw strong legal claims not being pursued or litigated in the Australian court system. For example, insolvency trustees fearful of burdening their estates with adverse costs were leaving such claims on the table. The insolvency practitioners began funding cases on behalf of these estates, allowing them to pursue and recover on successful claims in exchange for paying a return to the funders.

Soon after, the practice of litigation funding was challenged in the Australian court system as improper under the common law doctrine of champerty, which prohibited a disinterested party from intervening in a case in exchange for case proceeds. The Australia High Court disagreed, finding that litigation funding benefitted the judicial system by providing access to justice and leveling the playing field between parties that might otherwise have imbalanced resources. As a result, the practice became more commonplace, particularly for intellectual property litigation and international arbitration. Eventually, litigation funding began to take hold in the United States and the United Kingdom, becoming more prevalent after the financial crisis and continuing to grow exponentially in the last five or six years.

During recent years, numerous law firms have explored or adopted the practice, including Am Law 100 firms and over 200 firms in the U.S. Meanwhile, litigation funding has been adopted worldwide and is being utilized in Asia, South America, Europe, and other regions.

Litigation finance represents one of three major innovations in the law over the past few centuries. Among the first innovations were contingency arrangements, which originally were disallowed but are now permitted in many jurisdictions worldwide. Next was the adoption of insurance, which provides for risk sharing between clients and defendants on the defense side. The third innovation is litigation finance, which in many ways is the mirror image of insurance. Litigation finance involves risk sharing for plaintiffs, but without the funders controlling the litigation. This distinguishes litigation funding from insurance defense funding. Unlike a litigation funder, insurers can exercise control over litigation and the attorneys whose fees they pay, including the vendors they use, the travel arrangements they can make, their legal strategy, and even settlement.

C. Types of Litigation Finance

Litigation finance exists in both the commercial and consumer contexts. Commercial litigation finance provides funding for business or commercial disputes over a wide spectrum of subject matters and claims, such as intellectual property, patent infringement, breach of contract, antitrust, theft of trade secrets, fraud, breach of fiduciary duty, and others. Typically, these cases are business-to-business disputes involving sophisticated parties represented by sophisticated counsel. Commercial litigation funding is typically provided in high dollar disputes and the funder's investment often exceeds $1 million. While these agreements can take on many structures, as explained below, a commercial litigation funder most commonly invests capital to cover all or a portion of the legal fees and expenses in exchange for an interest in any future recovery from the lawsuit.

By contrast, consumer litigation funders typically finance personal injury and malpractice cases, as well as class actions and mass tort litigation. Recipients of consumer litigation funding are, as the name suggests, consumers. These individuals often have little or no prior experience with the legal system or complex agreements. Consumer litigants typically receive funding in the form of loans to cover legal costs and living and medical expenses during the pendency of their lawsuit. Often in consumer funding, the funder is paid out of the litigant's recovery at the end of the case in an amount based on interest charges and fees added to the funded amount.

D. Who Uses Commercial Litigation Finance?

Commercial litigation finance benefits a variety of businesses and individuals - both clients and their counsel. At its inception, litigation funding was primarily provided to small or mid-sized companies involved in "David versus Goliath" cases against larger, better-capitalized adversaries. Often in these situations, the smaller company – which in the patent context may be as small as a solo inventor – cannot afford to hire counsel as effective as its counterparty or even hire counsel at all. As a result, the company may forego asserting a claim or may have to litigate at a

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Challenges Presented by Litigation Funding

First appeared as part of the conference materials for the
28th Annual Advanced Patent Law Institute session
"Challenges Presented by Litigation Funding"