Third Party Litigation Investment/Financing

WHAT IS THIRD PARTY LITIGATION INVESTMENT/FINANCING?

Third party litigation investment (TPLI) is a practice where an external party, separate from the plaintiff and defendant, invests in a legal claim by providing money to one of the parties involved in exchange for a share of the settlement or judgment that exceeds the initial investment.

TPLI distorts the incentives in the system and introduces a financial motive that can prolong litigation and drive up the cost of settlements, wasting court and party resources for the sole purpose of extracting a larger return for the investors. Financial investors damage the attorney-client relationship by entering into financial arrangements with legal counsel in cases that then disturb the independent judgment of counsel.

Allowing outsiders to secretly use courtrooms to make an investment encourages the filing of non-meritorious litigation and the prolongation of litigation against the wishes of the parties themselves. Unlike attorneys, litigation investors do not owe a fiduciary duty to litigants and will act in their own best interests. The practice also spawns more litigation. There is clear evidence of litigation investors and their lawyers and clients litigating over proceeds of a lawsuit in private arbitration. There are also well-published examples of litigation investors preventing and objecting to "premature" settlements that the parties want.

WHY BAN TPLI IN NORTH CAROLINA?

In recent years, TPLI has experienced explosive growth and is now a multi-billion-dollar industry worldwide, with an estimated $15.2 billion in assets under management in the United States alone. It is prominent in venues such as New York, California, and Illinois and we know that financial investors are now trying to develop the North Carolina market.

In navigating the complex landscape of TPLI, the NC Chamber and aligned state partners seek to secure a significant legal win by **standing out among other states addressing TPLI through guardrails and advancing a bill that will ban the practice altogether. We must protect our national security and domestic companies from foreign adversaries and keep the civil justice system from becoming a financial investment market. The national security threat of adversaries like China finding intellectual property litigation is real.**

We believe the "market" in North Carolina is in its infancy and only know anecdotal stories of financiers coming to the state and visiting with law firms. Financial litigation investment agreements are private and secretive. We do know our largest law firms get approached by funders who have capital to invest on behalf of their investors.

WHAT DOES THE PROPOSED LEGISLATION DO?

The proposed ban on litigation investments **is neutral with regard to our current litigation system.** No ordinary practices are impacted whatsoever. The proposed ban merely will operate as a vaccine against the spreading virus of TPLI, which threatens to turn our North Carolina courts into a financial investment market, and which also will enable hostile adversaries to undermine our national security by seeking our intellectual property or seeking to distract our defense and technology companies with the burden of litigation.

WHAT ABOUT CHAMPERTY & MAINTENANCE?

Traditionally, the common law doctrines of maintenance and champerty prohibited non-parties from financing litigation in exchange for a share of the proceeds, but this doctrine is a common law doctrine that is being outstripped by financial innovation and its contours vary from jurisdiction to jurisdiction.

North Carolina courts still recognize the doctrines of champerty and maintenance but impose a high bar on what type of behavior is prohibited and the doctrines came into being long before the innovation of litigation investments. Under our state's longstanding caselaw, a third party does not violate these doctrines merely by sharing in a litigant's recovery. Rather, third-party involvement or funding is only prohibited if the **"purpose"** is to create "strife." *Odell v. Legal Bucks, LLC*, 192 N.C. App. 298, 665 S.E.2d 767 (2008) (emphasis added). This is a high standard and must be addressed on a case-by-case basis and will not prevent litigation investments nor turning civil litigation into an investment market.

THE NATIONAL MODEL FOR REGULATION:

1. **Disclosure** and transparency of TPLF in litigation.
2. **Consumer Protection** of the plaintiff so that the funder doesn't take their cut first or walk away with over half of the settlement amount.
3. **Anti-Steering:** Restrict Funders from **taking control** of lawsuits or deciding when to continue, settle, etc.
4. **Limit or prohibit** foreign entities from funding lawsuits in the U.S. to eliminate the **national security risk** of the practice.

- *NCOIL Model Act*, Transparency in Third Party Litigation Funding (November 24, 2024)
- *NBCSL Model Legislation*

MORE ON THE NATIONAL SECURITY RISK:

TPLI is a risk to national security. There is a growing concern that a large volume of foreign-sourced money may be pouring into U.S. courts via TPLI, raising significant national and economic security risks. By funding legal claims against U.S. companies, foreign adversaries are able to tie up and divert our business community's resources to costly and prolonged litigation and gain access in discovery to sensitive, confidential information. The limited information available because of the secrecy of the practice shows that sovereign wealth funds and non-U.S. citizens are participating in TPLI.

We do know that some foreign litigation funders have been uncovered: France, China, Russia (via Russian oligarchs bypassing sanctions), Saudi Arabia.

OUR SOLUTION

We believe legal claims and courthouses in this state are not financial markets for investments and are not vehicles for third parties to profit by financing a party to a civil proceeding for the purpose of obtaining and maximizing an investment return. Additionally, our courts should not be used to undermine our national security by hostile adversaries seeking our intellectual property or seeking to distract our inventors with the burden of litigation. The civil justice system in this state is not a financial market but is an instrument of justice and must remain distinct from financial markets. **It should be the policy of the state for it to be unlawful to engage in litigation investment in North Carolina.**

WHAT HAVE OTHER STATES DONE?

Delaware: The Chief Judge for the Delaware U.S. District Court has issued a standing order requiring the disclosure of TPLF.

Indiana: Mandates the disclosure of funding, prohibits funders from accessing proprietary data, and bans them from influencing or controlling lawsuits. (Enacted 2024) (Effective July 1, 2024) - HB 1160

Louisiana: Requires disclosure of TPLF agreements in civil cases before state courts, limits foreign litigation funding, and prohibits funder control or manipulation of litigation. (Enacted 2024) (Effective August 1, 2024) - SB 355

Montana: Requires disclosure of all TPLF agreements in civil cases before state courts and limits funders to a 25% cap in recovery. (Enacted 2023) - MCA 31-4-101 et seq. / SB 269

West Virginia: Expands transparency in litigation to large-scale litigation funding models. (Enacted 2024) (Effective June 7, 2024) - SB 850

Wisconsin: Requires disclosure of TPLF agreements in all litigation in state courts. (Enacted 2018) - Wis. Stat. §804.01(2)(bg) / AB 773

TPLF Bills pending: Federal HR1109, Arizona, Georgia, Iowa (full ban), Kansas, Maryland, Massachusetts, Mississippi, Nebraska, New Hampshire, New York, North Dakota, South Dakota, Ohio, Oklahoma

NC Chamber