The Attorney Professionalism Committee invites our readers to send in comments or alternate views to the responses printed below, as well as additional hypothetical fact patterns or scenarios to be considered for future columns. **Send your comments or questions to: journal@nysba.org, or NYSBA, One Elk Street, Albany, NY 12207, Attn: Attorney Professionalism Forum.**

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TO THE FORUM:

I am a partner at a law firm with experience representing clients who pay for my legal fees through litigation financing companies. In the past few years, more and more of my clients have used these services and, for the most part, our clients have been very pleased. Our firm has also been thrilled to get financed cases because many of our clients would not have commenced these cases if they had to pay the costs themselves even though they had legitimate claims.

A friend from college recently approached me about becoming an investor in a litigation financing company that he is starting. He knows that I have a lot of experience working in this area and that this industry has been taking off. He suggested that if I was able to refer clients to this company, we could all stand to make a lot of money and help out a lot of people.

Before I even consider my friend's proposal, I want to make sure I would not be violating any ethics rules. Can attorneys refer their clients (or potential clients) to litigation financing companies for assistance financing litigation? If so, can I refer a client to a litigation financing company where I am an investor? Would it matter if another one of my partners was handling the case and I had no involvement in it? Even if I don't become an investor, if I negotiate with litigation financing companies on my clients' behalf to finance one of my cases, am I able to charge the client for that work? When working with a litigation financing company are there any particular attorney-client privilege concerns I should be aware of? Does the litigation financing company have any ability to control the decisions or legal strategy of the case?

Sincerely,
Richie Referral

DEAR RICHIE REFERRAL:

Litigation financing is not something new. Various forms of litigation financing have been used in the United States since the 1980s. *See* Ethics Committee of the Commercial and Federal Litigation Section of the New York State Bar Association, *Report on the Ethical Implications of Third-Party Litigation Funding*, April 16, 2013 (citing Shepherd, Joanna M., *Ideal versus Reality in Third-Party Litigation Financing,* 8 J.L. Econ. & Pol'y 593 (Spring 2012)). "Third-party litigation financing (TPLF) describes the practice of providing money to a party to pursue a potential or filed lawsuit in return

for a share of any damages award or settlement." *Id.* In recent years, the number of private-practice lawyers using litigation financing has increased dramatically. *See* Joshua Hunt, *What Litigation Finance Is Really About*, The New Yorker, September 1, 2016. There are numerous ethical considerations surrounding an attorney's interaction with litigation financing firms and there are relatively few cases and ethics opinions in New York that address this rapidly developing area of professional responsibility.

As an initial matter, we caution that the legality of TPLF arrangements is an issue separate and apart from attorneys' ethical obligations and, of course, if a proposed action is illegal, then it would be unethical. *See* NYSBA Comm. on Prof'l Ethics, Op. 666 (1994) (citing NYSBA Comm. on Prof'l Ethics, Op. 498 (1978)).

REFERRING CLIENTS TO LITIGATION FINANCING FIRMS TO WHICH THE LAWYER OR ANOTHER ASSOCIATED LAWYER OWNS A FINANCIAL INTEREST

Referring your client to a litigation financing entity in which you or an associated lawyer have a financial interest implicates at least four of the conflict of interest rules within the New York Rules of Professional Conduct (RPC). *See* NYSBA Comm. on Prof'l Ethics, Op.1145 (2018).

RPC 1.8(a) "governs business transactions with clients. It is one of the most stringently enforced rules, and a violation of the rule often results in suspension or disbarment." Roy Simon, *Simon's New York Rules of Professional Conduct Annotated*, at 484 (2016 ed.). This rule sets forth the requirements that must be met in order for a lawyer to enter into a business transaction with a client where they have different interests in the transaction and the client would expect the lawyer to exercise professional judgment for the benefit of the client. *See* RPC 1.8(a). Notably, RPC 1.8(a) does not apply to traditional fee arrangements between a lawyer and client, such as a contingency fee arrangement, but the rule remains applicable when the lawyer accepts an interest in the client's business or other non-monetary property as payment for the lawyer's fee. *See* RPC 1.8 Comment [4C]. RPC 1.8(a) is triggered when a lawyer has a financial stake in the litigation financing firm because the client and the lawyer have differing interests with regard to the financing terms and it would be reasonable for the client to expect that the lawyer is exercising professional judgment on the client's behalf. *See* NYSBA Comm. on Prof'l Ethics, Op. 1145 (2018). When RPC 1.8(a) applies, the transaction must be "fair and reasonable to the client." *See id.*; RPC 1.8. If the transaction is fair and reasonable to the client, the lawyer must then comply with the other requirements of RPC 1.8(a) by: (1) making a full disclosure of the terms of the transaction in writing while utilizing language the client can understand, (2) advise the client in writing of the desirability of seeking independent legal counsel and providing the client with an opportunity to obtain it; and (3) obtaining informed consent from the client in a signed writing. *See* RPC 1.8(a)(1)–(3).

In accordance with RPC 1.10(a), even if you do not personally have an interest in the financing firm to which you refer your client, if any lawyer in your firm has an interest in the financing firm, the conflict is imputed to all of the lawyers in the firm. *See* RPC 1.10(a); NYSBA Comm. on Prof'l Ethics, Op. 1145 (2018). Rule 1.10(a) states, "[w]hile lawyers are associated in a firm, none of them shall knowingly represent a client when any one of them practicing alone would be prohibited from doing so by Rule 1.7, 1.8 or 1.9, except as otherwise provided therein." Therefore, it appears that compliance with RPC 1.8(a) will likely be possible in a litigation financing arrangement assuming the above criteria are met. *See* NYSBA Comm. on Prof'l Ethics, Op. 1145 (2018).

Even if you comply with all of the requirements in Rule 1.8(a), however, you must still comply with RPC 1.7(a)(2) which prohibits the representation of a client where a reasonable lawyer would conclude that "there is a significant risk that the lawyer's professional judgment on behalf of a client will be adversely affected by the lawyer's own financial, business, property or other personal interests." *See* RPC 1.7(a)(2). For example, this issue could arise when the financing firm has an interest in prolonging the litigation with the hope of enhancing the value of their investment, but it is in fact in the client's best interest to reach an early settlement. *See* NYSBA Comm. on Prof'l Ethics, Op. 1145 (2018). Conflicts associated with RPC 1.7(a) can also be waived, as long as the requirements of RPC 1.7(b) are met. RPC 1.7(b) permits representation when: "(1) the lawyer reasonably believes that the lawyer will be able to provide competent and diligent representation to each affected client; (2) the representation is not prohibited by law; (3) the representation does not involve the assertion of a claim by one client against another client represented by the lawyer in the same litigation or other proceeding before a tribunal; and (4) each affected client gives informed consent, confirmed in writing." Therefore, it also appears that compliance with RPC 1.7(a) will likely be possible in a litigation financing arrangement assuming the above criteria are met. *See* NYSBA Comm. on Prof'l Ethics, Op. 1145 (2018).

The next rule that is implicated is RPC 1.8(e), which prohibits a lawyer from advancing or guaranteeing financial assistance to a client. This rule is not something that

can be waived. This rule prevents clients from pursuing lawsuits that might not otherwise be brought and also prevents lawyers from having too great a financial stake in a litigation. *See* RPC 1.8 Comment [10]. RPC 1.8(e), however, does not prohibit a lawyer from advancing money for court costs and litigation expenses to a client. *See id*. These permitted advanced costs are often thought of as indistinguishable from contingent fee agreements and help ensure access to the courts. *See id.*

The fourth rule to consider is RPC 1.8(i) which prohibits a lawyer from acquiring "a proprietary interest in the cause of action or subject matter of litigation the lawyer is conducting for a client" with the exceptions of a contingency fee contract or a lien to secure fees and expenses. *See* RPC 1.8(i). This RPC is also designed to ensure the lawyer does not have too great an interest in the representation. *See* RPC 1.8(i) Comment [16]. In addition, if the lawyer acquires an interest in the litigation, it may make it more difficult for the client to discharge the lawyer. *See id.*

The NYSBA Committee on Professional Ethics opined that pursuant to RPC 1.8(e) and (i), it is not permissible for an attorney to refer a client to a litigation financing firm in which any attorney associated with that firm maintains a financial interest – and we agree. *See* NYSBA Comm. on Prof'l Ethics, Op. 1145 (2018). This conduct would likely be a violation of RPC 1.8(e) because the payments from the financing firm would amount to providing improper financial assistance to a client. *See id.*; NYSBA Comm. on Prof'l Ethics, Op. 666 (1994). In addition, the referral would also be in violation of Rule 1.8(i) because it would result in you or an associated attorney (albeit indirectly) having an improper financial stake in the client's litigation. *See id.* It is of little consequence that the attorney would not be providing the client with funds directly, or that the financing firm may have other investors, because RPC 8.4(a) specifically notes that a lawyer cannot violate the RPCs "through the act of another." *See* NYSBA Comm. on Prof'l Ethics, Op. 1145 (2018). Accordingly, we would strongly advise against referring a client to a litigation financing company where you or any attorneys in your firm are investors.

NEGOTIATING A CLIENT'S RELATIONSHIP WITH A LITIGATION FINANCING ENTITY

If your client requests assistance in negotiating an arrangement with a litigation financing firm, you are ethically allowed to assist in those negotiations and charge the client an additional fee for doing so. *See id.*; NYSBA Comm. on Prof'l Ethics, Op. 769 (2003). That said, you should consider whether you have any new obligations to the client as a result of the expanded representation. For example, consider having a separate engagement letter associated with the negotiation of the ligation financing relationship. *See* NYSBA Comm. on Prof'l Ethics, Op. 769 (2003). The NYSBA Committee on Professional Ethics has also suggested that the lawyer should consider that by negotiating the transaction, the client may reasonably assume that the lawyer is also endorsing the transaction and its terms. *See id.* Therefore, the lawyer should either disclaim responsibility or advise the client of all the costs and benefits of the transaction including alternative options. *See id.*

WHO IS PERMITTED TO CONTROL THE LITIGATION STRATEGY?

Your question concerning who may control the litigation strategy once a litigation financing firm becomes involved is a concern that has been raised by many. Some specific common concerns include: Who "owns" the claims? Who can control the lawsuit? How are conflicts resolved between the client's directions and the financing company's goals? *See* Ethics Committee of the Commercial and Federal Litigation Section of the New York State Bar Association, *supra*, at 9.

The RPC explicitly prohibits a litigation financing firm from directing or regulating the lawyer's professional judgment. RPC 5.4(c) states, "Unless authorized by law, a lawyer shall not permit a person who recommends, employs or pays the lawyer to render legal service for another to direct or regulate the lawyer's professional judgment in rendering such legal services or to cause the lawyer to compromise the lawyer's duty to maintain the confidential information of the client under Rule 1.6." RPC 5.4(c). As Professor Simon notes, "[e]ven if a client consents to allow a third party to pay his legal fees, the lawyer is still forbidden to let the third party 'direct or regulate' her professional judgment on behalf of the client unless authorized by law (as in the case of an insurance company)" and the burden is on the lawyer to prevent such interference. Roy Simon, *Simon's New York Rules of Professional Conduct Annotated*, at 1436 (2016 ed.). RPC 1.8(f) also provides that while a lawyer is permitted to accept compensation from a third party, the lawyer must obtain the client's informed consent, protect the client's confidential information (in accordance with RPC 1.6), and not allow that third party to interfere with the lawyer's professional judgment. *See* RPC 1.8(f). Therefore, in accordance with the RPC, the lawyer is not permitted to allow any third party to interfere with the lawyer's professional judgment despite payment of the lawyer's fees by a third party.

CONFIDENTIALITY CONSIDERATIONS WHEN REFERRING CLIENTS TO LITIGATION FINANCING ENTITIES

We have run out of space so you will have to wait until next month for the answer to your question about preserving attorney-client privilege with litigation financing companies. We will address the privilege issue and also answer a new question in the next Forum.

Sincerely,

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QUESTION FOR THE NEXT ATTORNEY PROFESSIONALISM FORUM:

A commercial client recently approached me about New York's adoption of the Compassionate Care Act (CCA), which permits the possession, use and distribution of medical marijuana in New York in certain circumstances. I have worked extensively on Department of Health legal issues and other aspects of the medical industry in the past, but I have no experience with the legalization of marijuana. After I started looking into the New York law for my client, I thought about a recent news article discussing how the federal marijuana laws conflicted with various state laws. It suddenly dawned on me: Am I assisting an illegal drug operation?

I certainly don't want to break any laws or risk losing my license to practice law. Even an *allegation* of being complicit in an illegal drug operation would be disastrous for my career. I also don't want to assist my client in breaking any laws. I feel very strongly, however, that an inconsistency between state and federal laws is a minefield for my client to navigate even with legal representation. This is a relatively new law with little precedent and guidance for its enforcement. At the same time, due to its politically charged and divisive subject matter, I imagine that there will be strict enforcement of the statute. I can't imagine telling any client that as a New York lawyer I am prohibited from giving him any advice about complying with a New York law!

Am I violating any rules of professional conduct by providing legal advice to my client on the CCA? Are there any limitations on what aspects of a marijuana business I can advise my client? If the policies for federal enforcement of marijuana laws change, will my ability to advise clients on the CCA also change? If my client starts to pay my legal fees from income derived from a marijuana business, am I permitted to accept those fees? Are there any other pitfalls I should be considering when advising a client on a marijuana business?

Sincerely,
Cheech N. Chong