Hon. Clint Bolick, Justice
Arizona Supreme Court
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IN THE SUPREME COURT OF THE STATE OF ARIZONA

In the matter of:	)	
	)	
PETITION TO AMEND RULE 8, RULES	)	Supreme Court No. 25-_____
OF CIVIL PROCEDURE	)	
___________________________________	)	

Pursuant to Rule 28 of the Rules of the Supreme Court, Petitioner respectfully petitions this Court to amend Rule 8, Rules of Civil Procedure, as shown in the Appendix, to add a new subsection (j) to require certain disclosures when litigation is subject to a litigation funding agreement.

I. Background

The Task Force on Alternative Business Structures ("Task Force") was established on March 18, 2024 by then-Chief Justice Robert Brutinel, by the entry of Administrative Order No. 2024-51. Among other tasks, the order directed the Task Force to evaluate the program allowing for the creation of Alternative Business Structures (ABS's), propose amendments to court rules as appropriate, and determine whether additional disclosures should be made for those funding ABS's.

On July 3, 2024, Chief Justice Ann A. Scott Timmer issued Administrative Order No. 2024-136, ordering the Task Force to examine third-party funding of civil litigation and its ramifications for ABS's. The order directed the Task Force to include any related proposals in its report and recommendations.

The Task Force submitted its report and recommendations to the Arizona Judicial Council (AJC) at its October 2024 meeting, at which time a motion was passed to accept the report and have the Task Force return to the December AJC meeting with a draft of the proposed rule amendments relating to third-party litigation funding of civil litigation. Proposed amendments to Civil Rule 8 were presented to the AJC at its December 2024 meeting, and a motion was passed to approve the filing of this petition reflecting the proposed amendments to Civil Rule 8 as set forth in the Appendix.

II. Background and Discussion

Generally speaking, third-party litigation funding is a practice by which a non-party provides funding to a litigant or law firm for profit or some other motivation. The type of third-party litigation funding the Task Force was informed about consisted of a non-recourse loan to the attorney, client, or both, with the repayment coming from the litigation recovery. Under such arrangement, the return to the funder can be calculated as a percentage of the recovery or based on a return of the principal advanced plus a rate of interest.

In an attorney-funder arrangement, the funder invests directly with the attorney or law firm. The funder provides capital for litigation expenses and some or all the attorney's fees in exchange for a share of the recovery.

In a typical client-funder arrangement, the funder provides capital to the client. The client agrees to compensate the funder from the recovery of the lawsuit. However, some client-funder litigation funding involves amounts paid to fund the living and medical expenses of a personal injury plaintiff and not necessarily to support the funding of the lawsuit itself.

A third and more recent type of funding is portfolio funding. This funding can be provided to clients involved in multiple actions, or to attorneys handling multiple actions involving different clients. The funding is structured around multiple claims in the form of cross-collateralization, meaning the funder's return is dependent upon the overall net financial performance of the portfolio as opposed to the outcome of each particular claim.

The Task Force heard from a multitude of speakers on several benefits, considerations, and concerns regarding third-party litigation funding. Most of the Task Force members acknowledged the importance of third-party litigation funding in providing access to justice but believed existing ethics rules can address most of the issues related to third-party funding.

Nonetheless, one of the concerns raised pertains to conflicts of interest, which can manifest in different ways. For example, when third-party litigation funders invest in a portfolio of cases, they may end up funding a litigant that is adversarial to another client. This may create a situation where an attorney must choose between his obligation to a client and the availability to access future funding.

Another example is that there may be a witness or judge who has a financial investment with the funder which may change the witness's incentive to testify truthfully or call into question the judge's impartiality. A third example is a rival business that may fund litigation against a competitor for the sole purpose of harassment or to obtain privileged information or trade secrets through the discovery process. Attorneys involved in cases with third-party funding must navigate complex ethical rules regarding conflicts of interest, confidentiality, and client communication.

The Task Force discussed what, if any, level of disclosure third-party litigation funding should have. While the Task Force advised against undue constraints on such funding or its providers, it recommended limited initial disclosure in cases involving third-party funding. This approach serves two key purposes: alerting the court to protect client interests, especially in class-action cases, and notifying opposing parties of potential conflicts. Essential disclosures include the existence of third-party funding and the funder's identity. If concerns arise, the court or opposing parties can request further information or safeguards.

Most members of the Task Force concluded that third-party litigation funding agreements should not be subject to initial disclosure. While some argue these agreements should be disclosed like insurance contracts, the Task Force believed they are different. Insurance contracts are often standard and relevant to settlement negotiations, whereas third-party litigation funding agreements involve internal business practices and litigation strategy, potentially protected by attorney work-product privilege. However, courts can review these agreements *in camera* or disclose them to opposing parties if there is good cause. The proposed amendments to Rule 8 as set forth in the Appendix reflect these considerations.

III. Proposed Amendments

Many jurisdictions, both state and federal, have either enacted or attempted to enact regulations on third-party litigation funding, and some courts have issued case-specific or standing orders related to litigation funding disclosure. The interests and concerns discussed above can be directly linked to specific factors in any litigation or arbitration. This is crucial because judges should not have to evaluate the abstract concept of disclosure.

For consistency, courts should have clear rules governing third-party litigation funding. Petitioner therefore proposes an amendment to Civil Rule 8, as shown in the Appendix, to create a new subsection (j) to establish initial disclosure provisions related to the existence of a third-party litigation funding agreement.

The Task Force recognized the importance of collecting relevant and readily available data on third-party funding. Therefore, proposed subpart (j)(1) requires a party whose litigation is subject to a third-party litigation funding agreement to separately file a certificate at the same time the party files the complaint or answer, or within seven days of entering the agreement. Such a filing will put the other party and the court on notice of the existence of a third-party litigation funding agreement. It will also help with data tracking through the court's case management system because the certificate, since filed separately, will have its own docket entry.

Proposed subpart (j)(2) provides a definition of "Third-Party Litigation Funding" or "Third-Party Litigation Funding Agreement" that largely tracks the definition from the Task Force's report and recommendations and establishes the types of funding agreements that would be subject to the disclosure requirements of this new subsection (j).

Proposed subpart (j)(3) establishes the information that must be included on the certificate, which includes:

- The name and address of any funders;
- The place of formation for any funder that is a legal entity;
- The nature of the financial interest of each funder in the litigation;

- Whether approval by any funder is necessary for litigation or settlement decisions and, if so, the nature of the terms and conditions relating to that approval; and
- Whether the funding is applicable to a portfolio of cases or is specific to the litigation at hand.

The certificate must also be signed by the party or its counsel attesting that the statements in the certificate are accurate to the best of the signor's knowledge, information, and belief and be in the form or a form substantially similar to the certificate adopted by the Director of the Administrative Office of the Courts. The latter requirement is to ensure consistency and completeness of the information provided, and will assist with data tracking.

Many members of the Task Force opined that courts should have flexibility to employ various methods such as *in camera* or *ex parte* submissions, redactions, sealing parts or the entire funding agreement, or requesting attorneys to certify representations about the contents of an undisclosed agreement. Proposed subpart (j)(4) addresses these considerations and provides that only in extraordinary circumstances may the court order the funding agreement, or any portion thereof, to be disclosed. Even so, an *in camera* review is required before the court can order disclosure, and the court must determine: (1) the disclosure will not run afoul of the work-product privilege, (2) the party seeking the agreement shows a substantial need, and (3) no less intrusive option is feasible. The proposed subpart further provides that any documents the court orders to be disclosed must be maintained as confidential by the receiving party, and that party is prohibited from further distributing such documents. The purpose of this subpart is to provide the parties with the necessary information without compromising sensitive or privileged information that may be contained within a funding agreement.

IV. Request

Petitioner believes that the proposed amendments fairly balance the parties' interests with the need to maintain the integrity of the judicial process and facilitate judicial efficiency. Petitioner therefore respectfully requests that this Court open this petition for public comment, consider the petition and comments in the regular course provided by Supreme Court Rule 28, and adopt the proposed amendments as set forth in the Appendix.

RESPECTFULLY SUBMITTED this 8th day of January, 2025.

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Appendix

(New language is <u>underlined</u>)

Rules of Civil Procedure

Rule 8. General Rules of Pleading
(a) through (i) [No change]
<u>(j) Third-Party Litigation Funding Agreements.</u>

<u>(1) *Generally*. A party whose litigation is subject to a third-party litigation funding agreement must separately file a certificate regarding third-party litigation funding at the same time the party files the complaint or answer. If a party's litigation was not subject to a third-party litigation funding agreement at the time of filing but becomes subject to a third-party litigation funding agreement during the pendency of the litigation, the party must file a certificate regarding third-party litigation funding within seven days of entering the agreement and serve a copy to all other parties.</u>

<u>(2) *Definitions*. For purposes of this rule, "Third-Party Litigation Funding" or "Third-Party Litigation Funding Agreement" means a third party enters into an agreement to provide funding for the purpose of pursuing or defending (which includes but is not limited to legal filings, appeals, testimony, discovery, retention of experts, preparing and drafting legal documents, creating a litigation strategy, and other related litigation expenses) a civil action, administrative proceeding, claim, cause of action, or a portfolio of cases, where the funder secures a financial interest in or benefit from any potential recovery. However, it does not include:</u>

<u>(A) loans, agreements, contracts, or arrangements to pay expenses that require repayment regardless of the outcome of the litigation;</u>

<u>(B) loans, agreements, contracts, or arrangements for personal needs or medical treatment of a party unless the purpose for doing so is to enable the pursuit of a claim;</u>

<u>(C) funding received from an entity or insurer with a preexisting contractual obligation to indemnify or defend a party to the action or a health insurer which has paid, or is obligated to pay, any sums for health care for an injured person under the terms of any health insurance policy, plan, or agreement; and</u>

<u>(D) a contingent fee agreement between a party and its counsel for legal services as permitted by the Rules of the Supreme Court.</u>

<u>(3) *Requirements*. The certificate regarding third-party litigation funding must:</u>

<u>(A) identify the name and address of any funders;</u>

(B) identify the place of formation for any funder that is a legal entity;
(C) identify the nature of the financial interest of each funder in the litigation;
(D) identify whether approval by any funder is necessary for litigation or settlement decisions and, if so, the nature of the terms and conditions relating to that approval;
(E) indicate whether the funding is applicable to a portfolio of cases or is specific to this litigation;
(F) be signed by the party or its counsel attesting that the statements in the certificate are accurate to the best of the signor's knowledge, information, and belief; and
(G) be in the form or a form substantially similar to the certificate adopted by the Director of the Administrative Office of the Courts.

(4) *Additional Disclosures*. For good cause shown, the court may order additional disclosures, including *ex parte* submission of the third-party litigation funding agreement to the court for an *in camera* review. In extraordinary circumstances and only after an *in camera* review, the court may order a party to provide the third-party litigation funding agreement, or any portion thereof, to the other party if the court determines the disclosure will not run afoul of the work-product privilege, the party seeking the agreement shows a substantial need, and then only if no less intrusive option is feasible. Any documents the court orders to be disclosed must be maintained as confidential by the receiving party, and that party is prohibited from further distributing such documents.