<u>Testimony of John H. Beisner[1]</u>
<u>On Behalf of the U.S. Chamber Institute for Legal Reform</u>
<u>Before the Subcommittee on the Constitution</u>
<u>of the Committee on the Judiciary</u>
<u>United States House Of Representatives</u>

<u>Hearing – Can We Sue Our Way to Prosperity?:</u>
<u>Litigation's Effect on America's Global Competitiveness</u>

<u>May 24, 2011</u>

Good afternoon Chairman Franks, Ranking Member Nadler and Members of the Subcommittee. Thank you for inviting me to testify today on behalf of the U.S. Chamber Institute For Legal Reform about the effects of litigation on the global competitiveness of U.S. companies.

The U.S. Chamber Institute for Legal Reform (ILR) is an affiliate of the U.S. Chamber of Commerce dedicated to making our nation's legal system simpler, fairer and faster for everyone. Founded by the Chamber in 1998 to address the country's litigation explosion, ILR is the only national legal reform advocate to approach reform comprehensively, by working to improve not only the law, but also the legal climate. The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than three million businesses and organizations of every size, sector and region.

Today's hearing asks a critical question that goes to the heart of ILR's mission: can we sue our way to prosperity? The answer to that question is a resounding no. America's litigious nature has caused serious damage to our country's productivity and innovation.

In recent years, we have made substantial strides in addressing certain forms of litigation abuse in the United States, both at the federal- and state-court levels. But while some problems have been corrected, new problems have emerged. And other, long-standing problems have continued unabated.

What is wrong with our judicial system? Why is it so prone to abuse? The root cause is that we have created incentives to sue – and to invest in litigation – instead of establishing disincentives for invoking judicial process unless absolutely necessary. Other countries discourage litigation; we nurture it.

When our nation was founded, Thomas Jefferson expressed the belief that the nation's highest duty was to "do equal and impartial justice to all citizens." But citizens and justice are

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now becoming largely irrelevant in the litigation process. In far too many lawsuits, citizens are simply pawns in an enterprising attorney/investor's business model, the goal of which is not to achieve justice for the citizen, but rather to secure profits for the attorney/investor. And from whom is that profit to be extracted? The American businesses that have built our economy.

Every year, this assault has grown more intense, with plaintiffs' counsel spinning increasingly marginal (if not downright frivolous) theories into threats of substantial liability. American businesses must divert both their personnel and financial resources from constructive efforts (including job creation) to defend against these efforts to loot their coffers. And the result has been a significant weakening of American competitiveness and a drain on our nation's economy.

The types of litigation abuse we continue to face in the U.S. are too numerous to catalog, but I would like to highlight four specific areas in which we are still seeing substantial litigation abuse: (1) fraud, lawyer screenings and improper client-recruitment efforts; (2) the importation of foreign claims into U.S. courts; (3) private lawsuits that piggyback on government investigations; and (4) aggregate litigation. In addition, I would like to address a growing practice – known as third-party litigation financing – that threatens to exacerbate all of these problems by making unlimited amounts of money available to litigants and attorneys who commit these abuses.

I. FRAUD, LAWYER SCREENINGS AND IMPROPER CLIENT-RECRUITMENT EFFORTS

Given the lucrative potential of private lawsuits in the U.S., it is not surprising that fraud has crept into the system. One notable example is the fraud that has occurred with respect to asbestos bankruptcy trusts. In addition, some lawyers have engaged in questionable tactics to recruit clients – tactics that have encouraged the filing of frivolous or fraudulent claims. The most notorious of these efforts have been the massive screening programs undertaken in the silica and welding-fume litigation, both of which resulted in the mass filing of meritless and even fraudulent claims – and forced defendants to spend huge sums of money defending themselves against groundless allegations. In addition, more and more lawyers are using the internet to troll for clients and sow dissatisfaction with products, in the hopes of generating large bodies of claims against targeted defendants. These efforts have contributed to the deluge of meritless lawsuits that clog the civil justice system.

A. Asbestos Bankruptcy Trusts And Fraud

One area in which we are seeing very troubling instances of fraud involves recovery for asbestos claims. More than 50 bankrupt companies have created personal-injury settlement trusts to pay present and future asbestos claimants for their alleged injuries through section 524(g) of the federal bankruptcy code. These trusts compensate asbestos victims from the assets of companies that held the greatest share of responsibility for historic asbestos exposures in the

United States.[2] Collectively, they manage an estimated $30 to $60 billion in total assets – much of which is opaquely administered with little to no oversight.[3] The trusts, which are effectively controlled by a handful of national asbestos law firms, routinely fail to disclose critical payment information, including who they pay, how much they pay and the reasons for making such payments. This lack of transparency has led to fraudulent, inconsistent and duplicative claims practices that threaten to siphon money away from those with legitimate claims.[4]

In one such instance, an alleged mesothelioma victim obtained hundreds of thousands of dollars from bankruptcy trusts by submitting claims with false details, such as describing himself as a shipyard worker when he merely passed through a shipyard on his way to Japan in World War II – while at the same time claiming in a civil lawsuit that his mesothelioma was caused exclusively by smoking cigarettes.[5] The ability of claimants (and their lawyers) to "double dip" – i.e., to recover multiple times for the same injury – undermines the integrity and reputation of the U.S. legal system.

B. **Screenings And Fraudulent Litigation**

Over the last decade, a new form of litigation abuse – phony medical "screenings" – has also harmed the integrity of our civil justice system. These mass medical screenings are generally organized by a consortium of plaintiffs' lawyers at hotels and union halls, and have been used to generate massive numbers of plaintiffs in the context of silicosis, asbestos and fen-phen litigation.[6] Working off a list of supposed diagnostic criteria, well-compensated doctors often diagnose hundreds of individuals a day with diseases they never knew they had, often in a matter of minutes. In the silicosis litigation, for example, ninety-nine percent of the more than 9,000 plaintiffs involved in the litigation were diagnosed by the same nine doctors,[7] and one of those doctors performed 1,239 diagnostic evaluations in 72 hours – an average of less than 4

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[2] *See, e.g.*, http://www.kaiserasbestostrust.com/ ("The Kaiser Asbestos Personal Injury Trust was created in 2006 as a result of the confirmation of The Kaiser Aluminum & Chemical Corporation Chapter 11 Joint Plan of Reorganization. The Trust was created to process, liquidate and pay valid asbestos personal injury claims in accordance with the Kaiser Aluminum & Chemical Corporation Asbestos Personal Injury Trust's Amended Trust Distribution Procedures.").

[3] *See, e.g.*, *40 billion reasons why asbestos litigation will grow*, Southeast Texas Record (Jan. 12, 2009), http://www.setexasrecord.com/news/216807-40-billion-reasons-why-asbestos-litigation-will-grow.

[4] *See, e.g.*, Texas Civil Justice League, *H.B. 2034 Halts Abuses in Asbestos Lawsuits* (Mar. 3, 2011), http://www.tcjl.com/blog/abuses-in-asbestos-lawsuits; Daniel Fisher, *No Double Dipping*, Forbes (Oct. 17, 2006), http://www.forbes.com/2006/10/17/asbestos-double-dipping-biz-cz_df_1017asbestos.html; The West Virginia Record, *Reform Attacks Trust-Fund Abuse* (Mar. 5, 2010), http://www.wvrecord.com/arguments/225196-reform-attacks-asbestos-trust-fund-abuse

[5] *See* Fisher, *No Double Dipping*, *supra*.

[6] *In re Silica Prods. Liab. Litig.*, 398 F. Supp. 2d 563 (S.D. Tex. 2005); Lester Brickman, *Ethical Issues in Asbestos Litigation*, 33 Hofstra L. Rev. 833, 836 (2005) (stating that in the asbestos context "nonmalignant asbestos litigation today mostly consists of . . . a massive client recruitment effort accounting for 90% of all claims currently being generated and resulting in the screening of over 750,000 and perhaps as many as 1,000,000 'litigants' in the past fifteen years").

[7] *In re Silica*, 398 F. Supp. 2d at 580.

minutes per evaluation.[8] The logic behind this practice is simple economics: when lawyers amass hundreds or thousands of claims, the potential exposure from those suits is often enough to force the defendant(s) to settle – even when the claims are entirely lacking in merit.

Medical screenings turn our legal system on its head. If someone thinks he has been injured by a product, the normal course of action would be to visit his doctor, determine what's wrong, and then – if he thinks he has a claim – retain a lawyer. Medical screenings, by contrast, "discover" injuries in people who never saw any reason to visit a doctor until they were encouraged to do so by a billboard or advertisement. The would-be plaintiffs who participate in these screenings have strong incentives to invent or imagine the symptoms that the doctors are looking for. And the physicians hired by the lawyers obviously have strong incentives to find that many people have been injured.

The welding fume litigation illustrates how such recruitment practices have led to the filing of fraudulent mass tort litigation. In that litigation, a group of plaintiffs' lawyers got together in the early 2000s to sponsor medico-legal screenings of welders around the country. These attorneys ran ads on billboards, the internet, and on late-night TV, telling welders they could be eligible for money if they had ever experienced any of a list of generic symptoms, including headaches, insomnia, erectile dysfunction and tremors.[9] The attorneys teamed up with a few neurologists whom they paid up to $10,000 a day to set up shop in motels and union halls around the country to "diagnose" welders with an extraordinarily rare disease called "manganism." By the time this "screening" process had wound its way through the country (primarily the South), the attorneys had managed to drum up around 10,000 welders to file lawsuits in courts around the country.[10] According to "fact sheet" responses that all federal-court plaintiffs were required to complete, approximately 90% of all the plaintiffs claiming a diagnosis of manganism were diagnosed by a single neurologist after exams that took as little as five minutes.[11] And the overwhelming majority of those diagnosed with manganism never sought follow-up medical attention for their supposed illnesses.

As the litigation progressed, plaintiffs selected several cases that came out of the screening process for trial in which the individuals turned out to have lied in discovery or faked their symptoms.[12] In one instance, surveillance revealed that a man who claimed to be completely disabled could in fact carry groceries, walk unassisted and rake leaves.[13]

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8 *The Silicosis Sheriff*, Wall St. J. (July 14, 2005), at A10.

9 *See, e.g.*, Mary Ellen Egan, *Twitch & Shout*, Forbes (Jan. 9, 2006), http://www.forbes.com/forbes/2006/0109/046.html.

10 *See generally Ruth v. A.O Smith Corp.* , 2006 U.S. Dist. LEXIS 7361, at *11-12 (N.D. Ohio Feb. 27, 2006) (noting that "the spark leading to the great number of recently-filed lawsuits is the combination of the advertising and screening processes used by plaintiffs' counsel to identify potential claimants").

11 *See In re Welding Fume Prods. Liab. Litig.*, 2006 U.S. Dist. LEXIS 16407, at *32 (N.D. Ohio Apr. 5, 2006).

12 *See id.*; *see also* Egan, *Twitch & Shout*, *supra* ("In December [2005] the first two welding cases in a mass tort with 5,300 claimants imploded amid charges of faked injuries.").

13 *See In re Welding Fume*, 2006 U.S. Dist. Lexis 16407, at *18.

In August 2006, after several such cases were dismissed, the federal court overseeing the multidistrict litigation proceeding issued a case management order establishing a "trial certification" process to be used in identifying MDL trial candidates going forward.[14] The order required plaintiffs' counsel to conduct a thorough review of their clients' medical records in certain select cases. Following that review, plaintiffs' counsel in each selected case were obligated to "(again) interview [their] clients carefully to obtain information bearing on whether pursuit of the case to trial might be unwarranted; this interview must include an explanation to the client that making false statements under oath can carry substantial personal penalties, both monetary and immuring."[15] Once that review and interview process was complete, plaintiffs had to either "certify" that they intended to proceed to trial in each case, dismiss the case or move to withdraw as counsel.[16] The August 2006 Order made clear that this trial-certification process was intended to remedy the problem of plaintiffs dismissing cases "after all parties spent substantial amounts of time and money preparing to litigate" them.[17] These requirements led to the dismissal of thousands of claims, and currently, less than ten percent of the original 10,000 cases remain.

The welding fume litigation may sound like a success story for defendants, but it depends on how one defines "success." These mass dismissals did not occur until years into the litigation. That's a lot of money spent defending litigation that, at the outset, consisted almost entirely of frivolous claims.

C. Web-Based Client Recruiting And Product Disparagement

Not surprisingly, the internet has proven to be a goldmine for entrepreneurial plaintiffs' lawyers trolling for clients. Websites like www.whocanIsue.com allow individuals to select from a series of potential lawsuits on a drop-down menu, enter a zip code, and obtain the name and contact information of a lawyer who may take their claim. Personal-injury lawyers seeking to advertise on www.whocanIsue.com pay a membership fee to appear on the website, and then bid additional amounts to have their advertisements displayed to potential clients that have submitted responses to preliminary questions.[18] The results are highly successful – many attorneys report receiving nearly twice as many calls as usual as a result of the advertisement.[19] WhocanIsue.com is not the only website of its kind – other popular online lawyer referral services include SueEasy.com and LegalMatch.com.[20]

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14 *See* Order, *In re Welding Fume Prods. Liab. Litig*., No. 1:03-cv-17000, MDL Dkt. No. 1888 (N.D. Ohio Aug. 28, 2006).

15 *Id*. at 3.

16 *Id*.

17 *Id*. at 2.

18 Whocanisue.com, https://members.whocanisue.com/faqaspx.

19 *See* Am. Tort Reform Ass'n, Judicial Hellholes 2009-10 5 (2010).

20 Siobhan Morrissee, *Who Can You Sue? Click Here.* Time (Aug. 6, 2008), http://www.time.com/time/nation/article/0,8599,1829725,00.html.

Attorney advertising is not problematic in its own right, but plaintiffs' attorneys have also created misleading websites that are not obviously lawyer advertisements. These websites provide biased information about various topics ripe for litigation, including allegedly defective products, illnesses or wide-scale disasters. Because the design, content and URL addresses of these websites disguise them as a source of information rather than an advertisement, a consumer may not even realize that he or she is viewing lawyer propaganda. To make matters worse, these websites are often the top results on Internet searches of a product or controversy. For instance, some of the top Google results on the Chinese drywall[21] or asbestos[22] controversies are lawyer-sponsored websites.

Food-borne illnesses are another popular subject of these websites; www.about-ecoli.com informs readers about the symptoms, risks and treatment of e-coli, and provides current information about e-coli breakouts caused by specific food products.[23] The website is sponsored by Marler Clark, a law firm that specializes in lawsuits related to outbreaks of food-borne illness. This same law firm sponsors similar websites discussing other food-related illnesses, such as listeria[24] and hemolytic uremic syndrome.[25] Lawyers also solicit clients in the wake of wide-scale disasters. For example, following the Gulf of Mexico oil spill, plaintiffs' lawyers relied heavily on the Internet to recruit clients. Plaintiff law firms established websites such as www.gulfoilspilllitigationgroup.com[26] and www.offshoreinjuries.com[27] to advertise contingency-fee services, and offer prospective clients free case reviews and interest-free cash advances. Once again, individuals searching the internet for information about these disasters were just as likely to land on a law firm's website as a legitimate news or public interest website – and it is not immediately apparent from these websites that the "articles" they contain are in fact attorney advertisements.

II. TRANSNATIONAL TORTS: THE IMPORTATION OF FOREIGN DISPUTES INTO U.S. COURTS

Another troubling development in the American civil justice system has been the rise in foreign lawsuits with virtually no nexus to the United States. American courts attract foreign litigants because our legal system provides an advantageous forum for plaintiffs. The availability of contingency-fee arrangements, the general lack of a strong sanctions regime for frivolous claims, and the lack of a loser-pays rule work together to lower the bar for filing a lawsuit in the U.S. as compared to many other countries. Although these procedural features are

[21] Chinesedrywallproblem.com, www.chinesedrywallproblem.com.

[22] Mesotheliomanews.com, http://www.mesotheliomanews.com/asbestos/; http://www.asbestosrights.com/cigarettes.htm.

[23] about-ecoli.com, www.about-ecoli.com/.

[24] www.listeriablog.com.

[25] www.about-hus.com.

[26] www.gulfoilspilllitigationgroup.com.

[27] www.offshoreinjuries.com.

intended to make our court system accessible to people with legitimate claims, they also lead to abuse because there is virtually no downside to bringing a frivolous lawsuit in U.S. courts.

The following examples highlight two types of abuses involving foreign plaintiffs that have become increasingly commonplace in the U.S. judicial system: the rise in transnational tort lawsuits, and efforts to enforce foreign monetary judgments in U.S. courts.

Recent litigation involving the Dole Food Company highlights the problems posed to our legal system by transnational tort lawsuits. Claimants in these lawsuits alleged that exposure to Dibromochloropropane ("DBCP") on banana plantations caused the sterilization of thousands of banana harvesters. U.S. and Nicaraguan plaintiffs' attorneys joined forces to organize lawsuits against the defendant. They relied on local "captains" to identify potential plaintiffs and assist them in fabricating stories; plaintiffs' attorneys also fabricated employment documentation and medical evidence of sterilization.[28] In 2004, attorney Juan Dominguez filed three separate actions on behalf of banana workers in California state court. The cases were assigned to Judge Victoria Chaney, and *Tellez*, the first of these three cases, was designated as a test case to proceed before the others. Following a jury verdict in favor of plaintiffs, Dole discovered – and notified the court of – misconduct by the plaintiffs' attorneys in Nicaragua. Judge Chaney conducted a three-day hearing and dismissed the plaintiffs' claims, citing widespread fraud and the existence of a conspiracy among judges, medical labs and plaintiffs' attorneys in Nicaragua.[29] She further found that plaintiffs' lawyers abused the judicial process and cited a laundry list of ethical violations, including perjury, bribery and witness intimidation.[30] Judge Chaney dismissed plaintiffs' other cases with prejudice, stating from the bench that "each and every one of the plaintiffs in the *Mejia* and the *Rivera* cases have presented fraudulent documents and actively participated in a conspiracy to defraud this court, to extort money from the defendants, and to defraud the defendants."[31] Plaintiffs later appealed; as of July 2010, the judgment in *Tellez* was vacated and all direct actions have been dismissed.[32]

The 17 years of litigation between Ecuadorian plaintiffs and Texaco (later Chevron after the company acquired Texaco in 2001) serves as another vivid illustration of the abuses related to transnational litigation. There, foreign plaintiffs filed a series of lawsuits, claiming that the defendants employed improper by-product disposal techniques in their oil exploration operations, which led to the release of carcinogenic toxins within the Oriente region of the Amazon in Ecuador. The first lawsuit was filed in the Southern District of New York,[33] where plaintiffs sought relief under the Alien Tort Statute. Another group of plaintiffs filed a similar action in

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28 U.S. Chamber Inst. For Legal Reform, Think Globally, Sue Locally 26 (2010).

29 *Id.* at 28-29.

30 *Id.* at 28.

31 *Id.* at 29.

32 Press Release, Dole Food Co., Dole Food Co., Inc. Announces Los Angeles Superior Court Vacates Judgment and Dismisses Fraudulent Lawsuit Brought by Nicaraguans Claiming to Have Been Banana Workers (July 15, 2010), http://www.dole.com/CompanyInformation/PressReleases/PressReleaseDetails/tabid/1268/Default.aspx?contentid=11722.

33 *See Aguinda v. Texaco*, No. 93 Civ. 7527 (VLB) (S.D.N.Y. Apr. 11, 1994).

Ashanga Jota v. Texaco.[34] The District Court for the Southern District of New York consolidated the two lawsuits. The judge presiding over the cases dismissed the lawsuits on *forum non conveniens* grounds.[35] After these lawsuits were dismissed, plaintiffs filed two more lawsuits, one in federal court in San Francisco and one in Ecuador. With respect to the lawsuit filed in San Francisco, the court granted the defendant's motion for summary judgment and reprimanded the plaintiffs' attorneys for serious misconduct.[36] According to the court, the "case was manufactured by plaintiffs' counsel for reasons other than to seek a recovery on the[] plaintiffs' behalf."[37] The court explained that "[t]his litigation is likely a smaller piece of some larger scheme against defendants."[38] The pervasive misconduct carried out by the plaintiffs' attorneys in the litigation has led Chevron to bring its own lawsuit against the plaintiffs, charging them with seeking to "extort a multi-billion dollar payment from Chevron through fabricated evidence and a campaign to incite public outrage."[39]

In addition to transnational tort cases, the American civil justice system has also seen an uptick in efforts to enforce foreign judgments in U.S. courts. These enforcement proceedings are particularly egregious because they combine the worst aspects of certain permissive foreign laws with U.S. court procedures. Plaintiffs in some foreign jurisdictions are able to obtain judgments under substantive foreign laws that would not pass Constitutional muster here, and then take advantage of the United States' permissive rules encouraging lawsuit filing (e.g., no fee shifting and the availability of contingency fees) to file civil actions to enforce those judgments. U.S. courts should be reluctant to enforce these kinds of foreign judgments because they fly in the face of the public policy undergirding the American civil justice system: to provide compensation for injuries in a manner that comports with fundamental fairness and due process.

In the litigation involving Dole, a number of plaintiffs have attempted to enforce judgments issued in Nicaragua under Special Law 364 in U.S. courts.[40] Lobbying efforts by plaintiffs' lawyers were instrumental in the passage of Special Law 364, which specifically addresses the claims of individuals exposed to DBCP and includes numerous provisions that openly aid plaintiffs. But in 2007, a federal judge in Florida refused to enforce a $97 million judgment issued by a Nicaraguan Judge implicated in the conspiracy described by Judge Victoria Chaney in a related proceeding in California state court. The court reasoned that enforcing the judgment would violate both international due process and Florida public policy.[41] It stated that

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34 No. 94 Civ. 9266 (JSR) (S.D.N.Y. 1994).

35 *See Aguinda v. Texaco, Inc.*, 945 F. Supp. 625 (S.D.N.Y. 1996).

36 *See Gonzales v. Texaco, Inc.*, No. C 06-02820 WHA, Order Granting Motions for Summary Judgment and Terminating Sanctions (N.D. Cal. Aug. 3, 2007).

37 *Id.*

38 *Id.*

39 Ashby Jones, Chevron Turns Tables on Ecuador Plaintiffs; Sues Them, The Wall Street Journal Law Blog, Feb. 2, 2011, http://blogs.wsj.com/law/2011/02/02/chevron-turns-tables-on-ecuador-plaintiffs-sues-them/.

40 *See, e.g.*, *Sanchez Osorio v. Dole Food Co.*, 665 F. Supp. 2d 1307 (S.D. Fla. 2009); *Franco v. The Dow Chem. Co.*, 2003 WL 24288299 (C.D. Cal. 2003).

41 *Sanchez Osorio*, 665 F. Supp. 2d at 1352.

"the legal regime set up by Special Law 364 . . . does not comport with the basic fairness that the international concept of due process requires. It does not even come close. 'Civilized nations' do not typically require defendants to pay out millions of dollars without proof that they are responsible for the alleged injuries . . . [and] do not subject foreign defendants to the type of discriminatory laws and procedures mandated by Special Law 364."[42]

The dubious practice of enforcing invalid foreign judgments in U.S. courts is also well illustrated by the Chevron case. Plaintiffs filed suit against Chevron in Lago Agrio, Ecuador, alleging violations of Article 43 of the Environmental Management Act. The attorney representing the plaintiffs in this lawsuit had previously lobbied for the creation of the new law, which allows plaintiffs to sue in Ecuador for "environmental remediation of public land." Plaintiffs filed this lawsuit despite the fact that the Ecuador Constitution prohibits retroactive application of new laws, and the Environmental Management Act was enacted years after the conduct allegedly giving rise to plaintiffs' claims took place.

This past February, a judge in Ecuador ordered Chevron to pay $8.6 billion to clean up oil pollution and to pay twice that amount if the company did not publicly apologize in 15 days.[43] Chevron has not issued any such apology. Instead, it moved to enjoin the multi-billion-dollar judgment in the Southern District of New York. On March 7, 2011, U.S. District Judge Lewis Kaplan granted a preliminary injunction enjoining enforcement of the Ecuadorian judgment.[44] In so doing, Judge Kaplan recognized that the Chevron litigation was an "extraordinary case."[45] Judge Kaplan also recognized that the enforcement strategy chosen by the plaintiffs' attorney was devised with an eye towards coercing Chevron to settle the case so as to avoid any injury to its business reputation.[46] The court granted the preliminary injunction to protect Chevron from the "coercive effect of multiple proceedings . . . [and] distractions and other burdens of defending itself in multiple fora . . . ."[47] Judge Kaplan has also ordered the release of film outtakes from a documentary film about the controversy, which capture plaintiffs' attorneys and representatives organizing a conspiracy to pressure and intimidate judges in Ecuador, even going so far as to discuss the possibility of killing a judge if he ruled in favor of the defendant.[48]

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42 *Id*. at 1345.

43 *See* Chad Bray, *Chevron Lawyers Press for Injunction*, Feb. 18, 2011, The Wall Street Journal, http://blogs.wsj.com/law/2011/02/18/chevron-lawyers-press-for-us-injunction/.

44 *See Chevron Corp. v. Donziger*, 2011 U.S. Dist. LEXIS 22729 (S.D.N.Y. Mar. 7, 2011).

45 *Id.* at *4.

46 *Id.* at *92.

47 *Id.* at *93.

48 Mark Hamblett, *Circuit Finds 'Crude' Filmmaker Lacked Independence*, N.Y.L.J. (May 13, 2011) http://www.law.com/jsp/nylj/PubArticleNY.jsp?id=1202477931482&Circuit_Finds_Crude_Filmmaker_Lacked_Independence; The Amazon Post: Chevron's Views and Opinions on the Ecuador Lawsuit, *Caught on Tape*, Jan. 31, 2011, http://theamazonpost.com/category/caught-on-tape.

On May 12, 2011, a three-judge panel on the Second Circuit granted a partial stay to Judge Kaplan's preliminary injunction order.[49] The court left intact the portion of the order blocking the enforcement actions, but granted a stay as to the injunction preventing litigants from raising funds and discussing legal strategy.[50] The merits appeal on this matter is scheduled to be heard in late July or early August 2011.[51]

III. PRIVATE LAWSUITS THAT PIGGYBACK ON GOVERNMENT INVESTIGATIONS

Another troubling trend that is undermining the administration of justice is the filing of private civil lawsuits that follow on the heels of government enforcement proceedings, either while the government proceedings are still pending or after they have concluded. These "piggyback" lawsuits have no salutary effect on corporate conduct because the companies at issue have already been subject to an enforcement proceeding – and in many cases, have paid fines, penalties or disgorgement to the government, some of which has been disbursed to consumers or shareholders. Thus, these piggyback lawsuits often serve primarily to provide a way for plaintiffs' lawyers to feed off of government investigation efforts.

For many years, the most common form of "piggyback" litigation involved lawsuits in the wake of Federal Trade Commission ("FTC") investigations. As these cases proliferated, the FTC voiced concerns that they served mostly to enrich plaintiffs' lawyers – at the expense of injured consumers. Prior to the enactment of CAFA, the FTC even began filing amicus briefs opposing piggyback class actions. In explaining this practice, Commissioner Thomas Leary accused private attorneys of basically free-riding on the government's investigative efforts.[52] As he put it: "[t]he counsel . . . negotiate a settlement in which the class members receive nominal recoveries, the defendants are protected from future private lawsuits, and the plaintiffs' lawyers recover generous fees for very little work."[53] In other words, these cases effectively amounted to a transfer of wealth from a company to a class-action lawyer, with no real work accomplished by the plaintiffs' lawyer and no real benefit to the consumers on whose behalf the suit was supposedly brought.[54]

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[49] *Chevron v. Gerardo*, Nos. 11-1150-cv(L); 11-1264-cv(Con) (S.D.N.Y. May 12, 2011) (order granting partial stay of preliminary injunction).

[50] Mark Hamblett, *Circuit Stays Portion of Chevron Ruling*, N.Y.L.J. (May 13, 2011) http://www.law.com/jsp/nylj/PubArticleNY.jsp?id=1202493831985&Circuit_Stays_Portion_of_Chevron_Ruling&slreturn=1&hbxlogin=1.

[51] *Id.*

[52] Thomas B. Leary, *The FTC and Class Actions, Remarks at the Class Action Litigation Summit* (June 26, 2003), http://www.ftc.gov/speeches/leary/classactionsummitt.htm.

[53] *Id.*

[54] While some have sought to blame defense counsel (and to some extent, their clients) for agreeing to such settlements, that criticism cannot be justified. Defense counsel are under ethical obligations to zealously represent their clients (and, in turn, their shareholders). The responsibility for protecting the class interests lies exclusively with the purported class counsel, under the supervision of the court handling the matter.

More recently, the piggyback-litigation phenomenon has been most noticeable with respect to Foreign Corrupt Practices Act ("FCPA")[55] enforcement proceedings brought by the Department of Justice (the "DOJ") and the Securities and Exchange Commission (the "SEC"). These piggyback cases tend to fall into two categories: (1) shareholder class actions alleging that a company did not adequately disclose its FCPA exposure; and (2) derivative actions against officers and directors alleging that they failed to prevent a company from bribing foreign officials.[56]

Follow-on FCPA cases target companies at a difficult time. Companies going through DOJ or SEC FCPA enforcement proceedings often spend tens of millions of dollars, if not more, on attorneys and forensic accountants – on top of potentially multimillion-dollar criminal and civil fines and disgorgement – in order to determine whether their employees (often at a relatively low level) acted improperly. Enforcement proceedings also interrupt normal business operations, as companies make employees and documents available to lawyers, and take action against truly culpable employees. The investigations themselves are disclosable events and are almost always "bad news,"[57] resulting in negative publicity. Shareholder suits against companies involved in enforcement proceedings threaten to further delay the companies' ability to return to normal operations and to further damage shareholder value. These suits serve no purpose but to take money from current shareholders and transfer it to former (or other) shareholders – with a hefty slice cut out for the plaintiffs' lawyers.

Derivative shareholder suits are equally problematic in this arena. These suits tend to target senior officers and directors, not the employees who actually paid any bribes or condoned others paying them. The reason is simple enough: directors and officers are backed by the deep pockets of the company's D&O insurer; culpable employees have little money to pay in private civil damages, especially if they themselves have been the target of an individual enforcement proceeding.

Often, lawyers filing shareholder class actions against companies under investigation or derivative actions against directors and officers of a company under investigation do not even wait until the government investigation is complete.[58] Such tactics are particularly egregious, because they necessarily involve the company and senior management in defending against a

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55 15 U.S.C. §§ 78dd-1 *et seq.*

56 *See* Brian Grow, *Bribery Investigations Spark Shareholder Suits*, Reuters (Nov. 1 2010), http://www.reuters.com/assets/print?aid=USTRE6A04CO20101101; Priya Cherian Huskins, *FCPA Prosecutions: Liability Trend To Watch*, 60 Stan. L. Rev. 1447 (Mar. 2008). As an example of the first type of suit, *see Glazer Capital Mgmt, LP v. Magistri*, 549 F.3d 736 (9th Cir. 2008); Complaint, *In re Syncor Int'l Corp. Sec. Litig.*, 2004 WL 5784765 (C.D. Cal. 2004), *dismissed by In re Syncor Int'l Corp. Sec. Litig.*, No. CV-03-00052ABC (C.D. Cal. Dec. 3, 2008). As an example of the second type of case, *see Midwestern Teamsters Pension Trust Fund v. Baker Hughes Inc.*, 2009 WL 6799492 (S.D. Tex. 2009); *Hawaii Structural Ironworkers Pension Trust Fund ex rel. Alcoa, Inc.*, 2008 WL 2705548 (W.D. Pa. 2008).

57 Grow, *Bribery Investigations*.

58 *See, e.g.*, SciClone Pharmaceuticals, Inc., *Quarterly Report for the Period Ending March 31, 2011*, filed on Form 10-Q, at 10-11; Pride Int'l Inc., *Quarterly Report for the Period Ending March 31, 2011*, filed on Form 10-Q, at 12-13.

private civil suit – and in making strategic judgments regarding such defense – when their focus should be on resolving the government's investigation. Both the DOJ and the SEC have developed leniency policies for companies that actively assist in government investigations.[59] These policies acknowledge that U.S. government resources are limited, and that cooperating companies can materially assist the government in enforcing the law and protecting shareholders. As part of cooperating with the government, companies in FCPA investigations frequently investigate their own potential wrongdoing and self-report misconduct to the government. When companies and their senior officers and directors face personal civil liability in addition to any exposure to the DOJ and SEC, their judgments regarding what issues to investigate and what results to report to the DOJ and SEC necessarily will be affected, possibly to the detriment of the integrity of the government's investigation.

IV. AGGREGATE-LITIGATION ABUSE

Finally, although the enactment of the Class Action Fairness Act of 2005 ("CAFA") has dramatically reduced class-action abuse, several serious problems remain in the aggregate-litigation arena. Today, I will discuss three: (1) state attorney general actions; (2) the routine deprivation of due process in class actions that remain in state courts; and (3) mass joinder actions.

A. State Attorney General/Private Counsel Partnerships

A key driving force behind abusive aggregate litigation is the proliferation of arrangements under which state attorneys general ("AGs") hire outside counsel on a contingency basis to represent the state in civil litigation. This problem has been exacerbated by the fact that more and more federal laws give state attorneys general enforcement authority.[60] Attorney general-private counsel partnerships are promoted by AGs as a win-win situation, because such suits are prosecuted without using tax dollars. But AG contingency-fee litigation raises serious conflict-of-interest and other ethical questions – and it imposes other costs as well.

For one thing, these "[c]ontingency deals raise the question of whether state attorneys general are pursuing the public interest or merely rewarding campaign donors with lucrative business."[61] In addition, these cases pose a danger that is often far out of proportion to their merit, for several reasons.

First, juries understand that the AG is a public official, acting on behalf of the state, posing a significant risk that the jury will find the state's case credible regardless of the merits of the actual allegation. That might not be a problem if state AGs were fairly restrained about

[59] *See* United States Attorneys' Manual § 9-28; SEC Enforcement Manual § 6.2.

[60] For example, state attorneys general can enforce the Truth in Lending Act's mortgage mandates, 15 U.S.C. § 1640(e), and the Health Insurance Portability and Accountability Act's privacy provisions, 42 U.S.C. § 1320d–5(d).

[61] Richard O. Faulk & John S. Gray, *Alchemy in the Courtroom? The Transmutation of Public Nuisance Litigation*, 2007 Mich. St. L. Rev. 941, 969 n.141 (2007).

bringing enforcement actions, but unfortunately that is less and less the case. In recent years, multiple state AGs have pushed the legal envelope, pursuing untested legal theories against American businesses that thought they were operating within the law. For example, a state might sue a drug company over its advertising – advertising the FDA had approved – arguing that each of tens of thousands of sales of the drug violated state law. Obviously, one novel aspect of such claims is that they would hold drug manufacturers liable despite compliance with highly detailed and very stringent federal standards. Another novel aspect of these claims is their size. Many of these suits seek to aggregate what are really thousands of individual transactions – that occurred under different circumstances – in a single action. In that respect, these cases are prone to all the same abuses as class actions, without the protections afforded by class-certification requirements. But the most troubling aspect of these suits is that the state attorneys general involved essentially delegate their law-enforcement responsibilities to private profit-motivated attorneys. As one article aptly noted, "[t]he specific financial interest that the [outside lawyer] has taken in the litigation presents an inherent conflict between the goals of the state and the personal goals of the appointed attorney."[62]

Second, and relatedly, AG actions pose significant risks because they typically threaten substantial, even debilitating, costs to companies if they are successful. Most states authorize significant per-transaction penalties, and some state laws go even further, allowing AGs to seek full refunds for consumers, as well as attorneys' fees. In fact, some of these cases have produced verdicts of several hundred million dollars.[63]

A recent example of a private counsel partnership involved the hiring of a Houston-based law firm to prosecute a lawsuit against Janssen Pharmaceuticals with respect to the drug Risperdal in Pennsylvania. In that case, Pennsylvania alleged that the company had improperly marketed the drug for off-label uses not approved by the FDA. Such a suit ordinarily would have been brought by the state AG's office, but the Governor's Office persuaded the AG to grant it authority to bring the suit.[64] The Governor's Office then began contingency-fee negotiations with the Houston-based firm. During the same period, the firm's founding partner, F. Kenneth Bailey, made a number of substantial contributions to the then-governor's re-election campaign.[65] Janssen moved to invalidate the contingency-fee arrangement on several grounds, one of which was that the arrangement violated the company's due-process rights under both the state and federal constitutions. The Pennsylvania Supreme Court rejected Janssen's challenges,

62 David Edward Dahlquist, *Inherent Conflict: A Case Against the Use of Contingency Fees by Special Assistants in Quasi-Governmental Prosecutorial Roles*, 50 DePaul L. Rev. 743, 781 (2000).

63 *See, e.g.*, Hillary Russ, *La. Jury Hits J&J With $258M Verdict In Risperdal Suit*, Law 360 (Oct. 15, 2010), http://www.law360.com/topnews/articles/201824/la-jury-hits-j-j-with-258m-verdict-in-risperdal-suit (noting that jury returned a verdict of $257.7 million in suit brought by Louisiana Attorney General over alleged misrepresentations concerning the drug Risperdal); Becca Aaronson, *Medicaid Fraud Up? Or Is State Getting More Vigilant?*, Texas Tribune (Feb. 15, 2011), http://www.texastribune.org/texas-state-agencies/health-and-human-services-commission/medicaid-fraud-up-or-state-getting-more-vigilant/ (referencing Texas lawsuit against Actavis, which resulted in verdict of $170 million).

64 *See The State Lawsuit Racket, A Case Study in the Politician-Trial Lawyer Partnership*, Wall Street Journal Online (Apr. l8, 2009), http://online.wsj.com/article/SB123914567420098841.html.

65 *Id.*

finding that the company lacked standing to contest the state's hiring of the outside law firm.[66] Chief Justice Ronald D. Castille, writing for the majority, declared that "[p]ursuant to the plain language of Section 103 [of the Attorneys Act], Janssen, as a party to the action other than the Commonwealth party, cannot be heard to challenge [the outside law firm's] authority to represent the Commonwealth party."[67] Justice Saylor dissented, explaining that "Janssen forward[ed] a colorable argument that, to avoid actual impropriety or the appearance of partiality, due process requires the government's attorneys to be financially disinterested in the outcome of the litigation inasmuch as they are – ostensibly, at least – serving the public interest, and not their own personal financial interests."[68] Justice Saylor's dissent echoes widespread criticism of the contingency-fee agreement at issue in the *Janssen* case from many corners, including the Wall Street Journal.[69]

A lawsuit filed by the South Carolina Attorney General against AstraZeneca in 2009 similarly illustrates some of the problems posed by contingency-fee arrangements with outside counsel. In that case, South Carolina filed suit against AstraZeneca for its alleged off-label marketing of the drug Seroquel.[70] Under the terms of the contingency-fee agreement, the outside law firms would be entitled to 23 percent of any penalties awarded to the state under the South Carolina Unfair Trade Practices Act, while the attorney general's office would retain ten percent of the contingency fee under the agreement.[71] Because the AG and the state's outside counsel are apparently claiming that AstraZeneca must be penalized $5,000 for every Seroquel prescription ever written in South Carolina, the penalties could well "translate into 'at least millions' for the plaintiffs' firms."[72]

AstraZeneca has challenged this agreement in state court on two grounds. First, the company is claiming that the contingency-fee arrangement violates its due-process rights by allowing the attorney general to delegate his law-enforcement function to private plaintiffs' attorneys.[73] Second, the company also alleges that the attorney general has agreed to divide a "staggering" contingency fee among the outside counsel and the state. The lawsuit is currently pending.

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66 *See Commonwealth v. Janssen Pharm., Inc.*, 8 A.3d 267 (Pa. 2010).

67 *Id.* at 276.

68 *Id.* at 279 (Saylor, J., dissenting).

69 *See, e.g.*, Editorial, *The Pay-to-Sue Business: Write a Check, Get a No-Bid Contract To Litigate for the State*, Wall St. J. (Apr. 16, 2009), at A14, http://online.wsj.com/article/SB123984994639523745.html.

70 David Bario, *AstraZeneca Sues South Carolina to Block Use of Private Lawyers in State's Seroquel Case*, The National Law Journal, Mar. 17, 2011, http://www.law.com/jsp/cc/PubArticleCC.jsp?id=1202486359257&Sure_You_Can_Bring_Counsel_Of_Your_Choice_IF_We_Want_Them_Too.

71 *Id.*

72 *Id.* (citation omitted).

73 *Id.* AstraZeneca specifically characterizes the state's lawsuit as a "'law enforcement action akin to a criminal proceeding' under the guise of a civil suit." *Id.* (citation omitted).

Yet another example of private attorney-AG partnerships involves Oklahoma's "Big Chicken" lawsuit, filed in 2005, in which then-Attorney General Drew Edmondson hired the Tulsa-based firm Riggs, Abney, Neal, Turpen, Orginson & Lewis, to prosecute claims against chicken farms run by 14 major producers over alleged pollution of Oklahoma's waterways.[74] Recognizing the concerns raised by the arrangement, recently elected Governor Mary Fallin has announced plans to review it.[75]

Governor Fallin is not alone in her concerns. Several attorneys general have expressed the firm belief that this enforcement approach is ill-advised.[76] For example, the Attorney General of Colorado, John Suthers, has stated that his "office policy is not to hire outside lawyers on a contingency-fee basis when the state's police power is being asserted (such as when the state brings an action based on a claim of public nuisance or when bringing a consumer-protection action)."[77] In addition, several amendments have been introduced in the Senate that would bar state attorneys general from retaining private counsel to enforce federal laws on behalf of state AGs – or at the very least require disclosure of these arrangements.

More needs to be done, however, or AG-private counsel partnerships will continue to threaten the integrity of state enforcement actions.

B. State-Court Due-Process Violations

Although CAFA moved most class actions filed after 2005 to federal court, there are two groups of class actions that remain in state court. The first are pre-CAFA class actions (many filed on the eve of the legislation's enactment), which remain in state court because they are subject to pre-CAFA jurisdictional rules.[78] These cases represent the last hurrah of state-court class-action abuse, but continue to create problems six years after CAFA's enactment. The second are cases that fit within CAFA's "home state" and "local controversy" exceptions, which allow certain class actions to remain in state court as long as they satisfy specific criteria set forth in the Act.[79]

Unfortunately, many state courts continue to apply class-action standards in a manner that makes it impossible for defendants to get a fair day in court. Some state courts do this by

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74 *See Links to Okla. AG Land Lawyers Contingency Prize: Big Chicken*, Legal Newsline (Feb. 12, 2008), http://www.legalnewsline.com/news/207875-links-to-okla.-ag-land-lawyers-contingency-prize-big-chicken.

75 *See New Oklahoma Gov, AG To Review Arkansas Poultry Lawsuit*, http://www.hpj.com/archives/2010/nov10/nov15/1108NewOKagpoultrylawsuitre.cfm.

76 *See* Adam Liptak, *A Deal for the Public: If You Win, You Lose*, The New York Times (July 9, 2007) (noting that "[n]ot all state attorneys general have embraced contingent fees").

77 John Suthers, *Avoiding Contingency-Fee Land Mines: New Attorneys General Should Use Outside Counsel Only as a Last Resort*, The Washington Times, Dec. 2, 2010, http://www.washingtontimes.com/news/2010/dec/2/avoiding-contingency-fee-land-mines/.

78 Before CAFA, it was virtually impossible for defendants to remove most class actions to federal court (unless the named plaintiffs sought more than $75,000 in relief for themselves).

79 28 U.S.C. § 1332(d)(4)(A)-(B).

saying that the "predominance" requirement for class certification only requires that there be "some" common issues among the class.[80] This watering down of class-certification requirements essentially means that these courts certify classes even if the different class members' claims involve different facts. Such a result is grossly unfair to defendants because it means that a large group of plaintiffs can join together in one lawsuit even if some of their claims are much stronger than others – and that a defendant might end up liable to thousands of people who could never have proven their claims in individual trials.

Other courts have adopted various "presumptions" to support their conclusion that cases can be decided based on common evidence. For example, these courts might presume that everyone in the class heard an alleged misstatement or would have been affected by a statement in the same way, even if the facts show that the court's presumption is false.[81] Such "presumptions" give plaintiffs enormous leverage in state-court class actions by essentially relieving them of their burdens of proof. As a result, they often lead to the types of "blackmail lawsuits" that first spurred Congress to enact CAFA.

To make matters worse, once a class is certified, many state courts are making it virtually impossible for the defendants to defend themselves at trial. That's because these courts are effectively saying to defendants: "Sorry, this is a class action and you are therefore barred from introducing any individualized evidence at trial." So a defendant might be barred from showing that some consumers were not deceived by a supposed misrepresentation, or that some people's property value actually increased during the class period or that the named plaintiffs did not rely on a certain statement because those are "individualized" defenses rather than theoretical classwide defenses.

This problem has grown so vexing that Justice Scalia has raised the question whether some state-court class-action procedures are unconstitutional because they violate due-process principles. In *Philip Morris USA Inc. v. Scott*, the case that recently garnered Justice Scalia's attention, a Louisiana state appellate court upheld a $241 million class-action verdict in a case involving more than 500,000 Louisiana smokers who claimed to be deceived by the defendants' allegedly fraudulent marketing practices.[82] The state court of appeals found that the verdict was proper even though the trial court: (1) refused to allow defendants to exercise their due-process right to cross-examine the class representatives regarding the issue of causation; and (2) did not require plaintiffs to prove reliance – a well-recognized requirement of Louisiana state-law fraud claims – on behalf of all proposed class members. In essence, the Louisiana court used the class-

[80] *See, e.g.*, *Plubell v. Merck & Co*., 289 S.W.3d 707 (Mo. Ct. App. 2009) (class certification of consumer-fraud claims is appropriate under Missouri's class certification standard as long as there is "[a] single common issue" that applies to all proposed class members' claims); *see also Ark. Media, LLC v. Bobitt*, 2010 Ark. 76, 12 (Ark. 2010) ("[c]hallenges based on the statutes of limitations, fraudulent concealment, releases, causation, or reliance have usually been rejected and will not bar predominance satisfaction because those issues go to the right of a class member to recover, in contrast to underlying common issues of the defendant's liability").

[81] *See Curtis v. Altria Grp., Inc.*, 792 N.W.2d 836, 859 (Minn. Ct. App. 2010) (finding that causation can be "inferred" on a classwide basis in a consumer-fraud action where the defendant engaged in "extensive marketing" because there is a "commonsense inference that [defendant's] massive advertising campaign was successful").

[82] *Philip Morris USA Inc. v. Scott*, 131 S. Ct. 1 (U.S. 2010) (Scalia, J., in chambers).

action device – a product of a rule of procedure – to fundamentally transform the substantive law governing fraud claims. Recognizing the grave implications of *Scott*, Justice Scalia took the extraordinary step of staying the verdict until the Supreme Court rules on the defendant's petition for certiorari, noting that the order raised a "[n]ational concern" about abusive procedures in class actions in state court. Justice Scalia explained that the "apparent consequence of the Court of Appeal's holding is that individual plaintiffs who could not recover had they sued separately can recover only because their claims were aggregated with others' through the procedural device of the class action."[83] The Supreme Court is expected to indicate shortly whether it will hear this case.

Unfortunately, the *Scott* case is not unique. Last year, the West Virginia Supreme Court issued a similar ruling in *Perrine v. E.I. Du Pont de Numours & Co.*[84] In *Perrine*, the plaintiffs brought a purported environmental class-action lawsuit against DuPont and other businesses seeking damages and medical-monitoring costs associated with alleged exposure to hazardous substances from one of the largest zinc smelter facilities in the United States. In certifying the action, the trial court held that whether "the defendants' operation and management of the smelter site caused the contamination of the proposed class area" was a predominating common issue, and plaintiffs' claims could therefore be resolved on a classwide basis. On appeal, defendants argued that the trial court improperly ignored defendants' constitutional right to present individualized evidence and defenses at trial. The West Virginia Supreme Court disagreed and held: "to the extent that th[e] class action was properly certified by the trial court, all of [defendant's] individualized defenses have no merit."[85] In other words, as long as a class is certified in West Virginia, the defendant ***is not allowed*** to defend itself based on actual facts related to the actual plaintiffs or other class members. Instead, it can only defend itself based on theoretical or aggregate evidence, even if that evidence is divorced from reality. In his dissent, West Virginia Justice Menis Ketchum warned about the consequences of embracing such dubious class-action practice: "[T]he plaintiffs' lawyers from the DuPont case will wreak enormous economic harm on West Virginia's economy. They will collect millions in fees and return to their out-of-state residences leaving the West Virginia economy in shambles."[86]

C. Mass Joinder Litigation

Yet another area of ongoing abuse in the aggregate-litigation arena involves mass joinder actions, in which dozens of people who allege separate injuries join together in one lawsuit. These suits are similar to class actions, except that each individual is named in the complaint. To quote the Senate Report that accompanied CAFA:

> [M]ass actions are simply class actions in disguise. They involve a lot of people who want their claims adjudicated together and they often result in the same abuses as class actions. In fact, sometimes the abuses are even worse because the

[83] *Id.* at 3.

[84] 649 S.E.2d 815, 854 (W. Va. 2010).

[85] *Id.*

[86] *Id.* at 915.

> lawyers seek to join claims that have little to do with each other and confuse a jury into awarding millions of dollars to individuals who have suffered no real injury.[87]

Because the vast majority of these lawsuits involve cases with disparate facts and injuries – where the only thing in common is a shared defendant or product – mass actions pose serious due-process issues for defendants.[88] As one commentator succinctly put it, "[m]ass actions involve many plaintiffs, have high settlement value, and [are subject to] abuse."[89]

CAFA partially addressed the mass-action problem by creating federal jurisdiction over mass actions with 100 or more plaintiffs. The Act, however, did not address cases with fewer than 100 plaintiffs. Thus, 99 plaintiffs with dissimilar claims can often still join together in one lawsuit and insulate their claims from federal jurisdiction.[90] When defendants have sought to remove these cases to federal court on the ground that the plaintiffs' claims are not properly joined – and one plaintiff should not be able to spoil diversity for other plaintiffs with whom his case has little in common – they have not met with consistent success. In one case, the U.S. Court of Appeals for the Eighth Circuit concluded that dozens of plaintiffs could avoid federal jurisdiction simply by joining their claims with those of one plaintiff who did not satisfy diversity.[91]

The "mass action" jurisdictional loophole is often exploited to the great prejudice of defendants. In contrast to federal courts, which have almost uniformly rejected multi-plaintiff trials, state courts are more likely to embrace "mass action" cases as "efficient." The problem with such cases, however, is that "efficiency" comes at the expense of justice. No jury can possibly keep track of the separate facts that apply to dozens of plaintiffs' claims. Instead, juries often assume that the defendant must have done something wrong if so many plaintiffs are suing, and they set a per-plaintiff award based on a fictional, composite plaintiff, stitched together from the most compelling attributes of each plaintiff's separate case. When plaintiffs succeed in keeping their improperly-joined cases in state court, they are able to use the threat of such an unjust (but likely) outcome to extract large settlements that do not reflect the actual value the cases would have if they were brought individually.

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[87] S. Rep. No. 109-14, at 47 (2005).

[88] *See* Mark A. Behrens and Cary Silverman, *Now Open for Business: The Transformation of Mississippi's Legal Climate*, 24 Miss. C. L. Rev. 393, 398 (2005).

[89] Cheryl Nichols, *The Importance of Selective Federal Preemption in the U.S. Securities Regulatory Framework: A Lesson from Canada, Our Neighbor to the North*, 10 Chap. L. Rev. 391, 440 n.245 (2006); *see also* Jack B. Weinstein, *Compensation for Mass Private Delicts: Evolving Roles of Administrative, Criminal, and Tort Law*, 2001 U. Ill. L. Rev. 947, 969 (2001) ("Private mass actions are subject to abuse.").

[90] *See, e.g.*, Nicole Ochi, *Complex Litigation in California and Beyond: Are Consumer Class and Mass Actions Dead? Complex Litigation Strategies after CAFA and MMJTA*, 41 Loy. L.A. L. Rev. 965, 1011 (2008); Guyon Knight, *The CAFA Mass Action Numerosity Requirement: Three Problems with Counting to 100*, 78 Fordham L. Rev. 1875, 1900 (2010).

[91] *In re Prempro Prods. Liab. Litig.*, 591 F.3d 613 (8th Cir. 2010).

V. THIRD PARTY LITIGATION FUNDING

As the problems I have just discussed amply demonstrate, ours is arguably the most litigious society in the developed world. Our litigiousness results in large part from three characteristics of the U.S. civil-justice system that have generally been rejected in other countries: (1) we allow contingency fees; (2) we require both parties to pay their own attorneys' fees, even if they prevail at trial; and (3) there is a relatively low opportunity cost associated with filing frivolous litigation. Given the problems with the U.S. civil-litigation system that I have discussed, our system should be considering ways to reform these aspects of U.S. civil litigation in order to make plaintiffs and lawyers more accountable for filing frivolous claims – and to rid our courts of "jackpot justice." Instead, however, a new form of lawsuit funding is emerging – third-party litigation financing or TPLF. This form of funding will lower the bar to filing lawsuits even further, and if it is left unchecked, it will make the problems I have discussed today much, much worse.

TPLF describes the practice of providing money to a party to fund the pursuit of a potential or pending lawsuit. Most TPLF contracts resemble non-recourse loans: the borrower obtains money to pursue a lawsuit and is only required to repay the loan if he or she obtains a damages award at trial or settles on favorable terms. Three variants[92] of TPLF have emerged and are growing in the United States:

Consumer lawsuit lending generally involves loans to individual plaintiffs to finance small claims or provide living expenses. Typically, the financing arrangement is structured as a non-recourse loan, with monthly interest accruing on the principal amount of the loan at rates that generally range from three to five percent per month. Essentially, in this type of TPLF, the plaintiff sells his or her claim to the TPLF company in exchange for an up-front cash payment. If the plaintiff's claim is successful, the plaintiff repays the TPLF provider the money advanced, plus interest, as well as any additional fees specified in the funding contract.[93] However, if the case is resolved on terms that do not provide enough funds to cover the plaintiff's loan, the plaintiff still owes the full amount of the loan – in essence the plaintiff can end up in a worse position than if he or she had not filed the lawsuit and obtained the loan to begin with.

Direct funding arrangements with businesses involved in commercial litigation constitute the second type of TPLF in the United States. In this type of funding, the third-party financier's return is usually a portion of any recovery that the plaintiff-business receives from the resolution of the litigation, whether through final judgment or settlement.[94] The percentage of

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92 A fourth variant of TPLF, which exists in some foreign jurisdictions, but not yet in the United States, involves TPLF providers contracting with potential plaintiffs to file class actions – and then funding those suits through direct payments to class counsel. Class-action financing is potentially the most lucrative type of third-party funding. At least one TPLF provider that funds class actions overseas has announced plans to develop funding opportunities in the United States. *See IMF: Australia's Major Litigation Funder, Experienced, Cautious and Profitable, Moves into US, UK – Markets Ten Times as Large and With Huge Opportunities*, Australian Co. News Bites (May 14, 2010).

93 Steven Garber, *Alternative Litigation Financing in the United States*, 9-10, The Rand Corporation (2010), http://americanlegalfin.com/press/RAND%20Alternative%20Litigation%20Financing.pdf.

94 *Id.* at 13-16.

recovery the TPLF provider will charge turns on several factors, including the amount of money advanced, the length of time until recovery, the potential value of the borrower's case and whether the case settles or goes to trial. In this type of TPLF, the TPLF provider essentially invests money in the outcome of the company's lawsuit, betting that the lawsuit will be successful.

Direct loans to law firms, the third variant, involves the lending of money by financiers directly to plaintiffs' law firms. Often, these are non-recourse loans that the firm is obliged to repay only if its litigation is successful. However, if the litigation is successful, the firm must repay the loan at interest rates significantly higher than normal commercial lending.[95]

Although TPLF is not yet widespread in the U.S., it is playing an increasingly visible – and potentially harmful – role in U.S. litigation. The recent growth of TPLF in the United States results from a number of factors, including rising litigation costs and professional-responsibility rules that prohibit attorneys from paying clients' living expenses while litigation is pending.[96] In addition, as the value of traditional investments has dropped, investors have been attracted to new investment vehicles.[97] Recent high-profile plaintiffs' victories in lawsuits funded by TPLF providers, particularly in Europe and Australia, have fueled some investors' perceptions that investments in TPLF companies are safe and profitable. During better economic times, these same investors put their money in public companies. Now that those companies may be struggling financially, perhaps even as a result of litigation, investors are turning away from investing in them (and potentially creating new jobs) in favor of financing litigation, which will only damage those companies further.

Third-party litigation financing has at least four negative consequences for the administration of civil justice.

First, TPLF increases litigation costs at the expense of truly aggrieved plaintiffs, the defendant or both, because it inserts a new party into the litigation equation whose sole interest is its return on its investment. For instance, in recent litigation regarding 9/11 Ground Zero workers, one of the plaintiffs' firms representing the Ground Zero workers used a TPLF loan of the direct-to-law-firm variant. The firm then sought to pass along $6.1 million in interest on the borrowed funds to the plaintiffs. The plaintiffs' lawyers argued strenuously in support of their position, but the judge presiding over the settlement ultimately rejected it. "In the context of $150 million," the judge told plaintiffs' counsel, "I believe you can absorb $6 million." One of the lawyers complained after the hearing that the judge ruled against plaintiffs' counsel "for no other reason than it's 9/11." Assuming he was correct, it means that plaintiffs in other cases ***would*** be required to pay interest on their lawyers' loans ***in addition*** to attorneys' fees.

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[95] *Id.*

[96] Model Rules of Prof'l Conduct, R. 1.8(e) (2009) (a "lawyer shall not provide financial assistance to a client in connection with pending or contemplated litigation").

[97] *See* Jane Croft, *Litigation finance follows credit crunch*, Fin. Times (Jan. 27, 2010); *Attorneys Explore Third-Party Funding in Commercial Disputes*, N.Y.L.J. (June 3, 2010).

Similarly, the consumer-lending variant of TPLF harms consumers who do not understand the implications of a funding arrangement. In the federal Vioxx litigation, for example, a number of persons who were eligible for the settlement program established by Merck obtained loans from a lawsuit lender. When they received their money from the program and proceeded to "settle up" with the lender, some were surprised to receive demands for amounts that equaled – and in some cases even exceeded – their recovery. When the lender sought to enforce liens on the borrowers' settlement distributions, the judge noted that such loan arrangements were barred by the terms of the resolution program.[98] In the end, the lender recovered little more than the amounts advanced, but only because the judge was very vigilant and involved in the settlement distributions.

Second, TPLF increases the filing of ***questionable*** claims. Unlike attorneys working on contingency, who are inclined only to invest "sweat equity" in cases that are likely to succeed, TPLF companies are mere investors – and they base their funding decisions on the present value of their expected return, of which the likelihood of success at trial is only one component. In addition, and also in contrast to most attorneys, TPLF providers can mitigate their downside risk by spreading the risk of any particular case over their entire portfolio of cases, and by spreading the risk among their investors.[99] For these reasons, TPLF providers can be expected to have even higher risk appetites than attorneys, and to be more willing to back claims of questionable merit.

Third, TPLF prolongs litigation by deterring plaintiffs from settling unless the defendant's offer is sufficiently generous to provide them a recovery after paying off ***both*** their attorneys and their TPLF lender. A plaintiff who must pay a finance company out of the proceeds of any recovery can be expected to reject what may otherwise be a fair settlement offer, hoping for a larger sum of money.[100] This problem is illustrated by the ongoing litigation between a network-security company called Deep Nines and a TPLF provider that previously had backed Deep Nines's commercial litigation against a software company. Deep Nines retained the TPLF provider to finance patent litigation with an $8 million loan. Deep Nines had a strong case, and eventually, the case settled for $25 million. That seems like a hefty settlement. But after interest, attorneys' fees and other expenses, how much did Deep Nines actually get? $800,000 – about three percent of the total recovery. And here's the most remarkable part: the financing company wasn't satisfied with its share and it sued Deep Nines for even more

98 *See In re Vioxx Prods. Liab. Litig.*, MDL Docket No. 1657, Minute Entry (E.D. La. Jan. 7, 2010).

99 *Cf.* Maya Steinitz, *Whose Claim is This Anyway? Third Party Litigation Funding*, 95 Minn. L. Rev. (forthcoming 2011) (manuscript at 51).

100 *See Rancman v. Interim Settlement Funding Corp.*, 789 N.E.2d 217, 220-21 (Ohio 2003) (noting that the amount the plaintiff-appellant owed to litigation financiers was an "absolute disincentive" to settle at a lesser amount).

money.[101] That litigation is still pending, more than four years after Deep Nines first borrowed the money to finance its suit.[102]

Fourth, TPLF undercuts a plaintiff's control over litigation because the TPLF provider, as an investor in the plaintiff's lawsuit, inherently seeks to protect its investment, and will therefore try to exert control over the plaintiff's strategic decisions. Even when the TPLF provider's efforts to control a plaintiff's case are not overt, the existence of TPLF funding, especially of the consumer-lending and commercial-litigation variants, inherently subordinates the plaintiff's own interests in the resolution of the litigation to the interests of the TPLF provider. In some sense, the plaintiff becomes a bystander in his or her own case. CNN reported recently about a North Carolina woman who sued the owner of a basketball team for sexual assault. She rejected all of the defendant's settlement offers, even though her own attorney recommended she take them, and insisted on going to trial – which she lost. Why did she do it? Because, unbeknownst to her attorney, she had borrowed money from a TPLF provider and needed at least $600,000 if she won or settled to repay the TPLF provider, which was more than the defendant offered in settlement.[103] In sum, TPLF threatens to transform a system of justice that was designed to adjudicate claims by aggrieved parties into an investment market controlled by third parties.

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Our judicial system was established almost 250 years ago to secure justice for all Americans. But America's open-armed approach to litigation does not promote justice. Instead, we have swung open our courthouse doors to plaintiffs who peddle far-fetched and even fraudulent theories of recovery.

I commend the Subcommittee for holding today's hearing and urge you to begin a serious dialogue about how to address the problems I have discussed today – and what reforms are needed to restore a sense of responsibility and restraint in American litigation. To help inform the dialogue, the Subcommittee should first conduct rigorous oversight of problematic fraud and abuse in our civil-justice system, especially in the areas of asbestos bankruptcy trusts, transnational torts, and partnerships between state attorneys general and contingency-fee counsel to enforce federal statutes.

Congress has begun this effort with its consideration of the Lawsuit Abuse Reduction Act of 2011, or LARA, which would: (1) make Rule 11 sanctions mandatory where a party is found to have acted "for any improper purpose, such as to harass, cause unnecessary delay, or needlessly increase the cost of litigation";[104] and (2) abolish the 21-day waiting period, which

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[101] *See* Alison Frankel, *Patent Litigation Weekly: Secret Details of Litigation Financing*, The American Lawyer (Nov. 9, 2009).

[102] *See Altitude Nines, LLC, v. Deep Nines, Inc.*, No. 603268-2008E (N.Y. Sup. Ct.); *see also* Joe Mullin, *Patent Litigation Weekly: How to win $25 million in a patent suit – and end up with a whole lot less*, Nov. 2 2009, http://thepriorart.typepad.com/the_prior_art/2009/11/altitude-capital-partners-altitude-nines-v-deep-nines.html.

[103] *See* http://transcripts.cnn.com/TRANSCRIPTS/1002/18/ec.01.html.

[104] Fed. R. Civ. P. 11(b)(1).

currently enables plaintiffs to avoid accountability for Rule 11 violations by withdrawing their claims within 21 days. Other reforms might include:

- Regulating medico-legal screenings to ensure that they comport with commonly-accepted medical practice;
- Allowing discretionary appeals of orders denying dispositive motions and *Daubert* evidentiary rulings;
- Increasing lawyer accountability by fining or disciplining lawyers who fail to perform due diligence before filing lawsuits, continue prosecuting a lawsuit after learning that the claim or claims being asserted are invalid, or otherwise engage in frivolous litigation;
- Requiring transparency in 524(g) asbestos bankruptcy trusts;
- Barring or strictly regulating third-party litigation funding; and/or
- Barring or strictly regulating state attorneys general from retaining outside, contingency-fee counsel to enforce any federal laws.

Thank you again for inviting me to speak, and I will be happy to answer any questions.