GoSueMe: THE BROKEN PROMISES OF THIRD-PARTY LITIGATION FUNDING

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(with contributions from Patrick Quallich)

Forget cryptocurrency—there is another kind of investment making the news in recent years and creating major headaches for corporate defendants: litigation funding.

Third-party litigation funding (TPLF) sees investment firms providing money to cover plaintiffs' litigation costs. In return, investors get a portion of any damages. How big has it become exactly? As of 2022, litigation funders had more than $13 billion under management in the United States. It has objectively influenced the number of lawsuits filed and the number of settlements and verdicts reached. But does that mean it is advancing justice?

Some tout funding as a means for potential plaintiffs to pursue their claims against wealthier company defendants. Its supporters argue that it helps level the playing field by reducing financial barriers. Others, however, argue that it injects under-regulated interests into lawsuits' outcomes, increases frivolous claims, drags out litigation, and can even take advantage of the plaintiffs themselves.

While study of the topic is limited, the published research does point to some troubling effects on the judicial system and its ability to deliver a just outcome.

EFFECTS ON THE JUDICIAL SYSTEM

More Lawsuits – One study found that litigation funding increases the number of lawsuits and exacerbates court backlogs. The obvious reason is that funding is designed to help people bring lawsuits. It is unsurprising that a greater volume of cases can inundate courts, especially as the system continues to work through its pandemic surfeit. But, as explained below, litigation funding can also prolong the litigation process by disincentivizing settlements—leaving even more cases clogging the system as new ones flood in.

Slower Resolutions and More Trials – Because the funder's interest is strictly financial, one main risk-reduction strategy is for it to diversify, investing in a "portfolio of cases" in the hopes that a few of them return a large payout. To encourage larger returns, plaintiff attorneys make larger demands and agree to settlements less often, resulting in a longer process and more cases going to trial.

An empirical study offers evidence to that effect. By examining statistics on medical malpractice litigation duration and awards, the study demonstrated that funding was associated with a 60.5% increase in claim payment, a 140% increase in resolution duration, and a 35.7% decrease in the probability of settlement. These numbers are strong evidence that third-party interests disrupt the litigation process and inflate damages requests.

EFFECTS ON JUSTICE

Who Gets Litigation Funding? – Litigation funding proudly claims to give the everyman access to justice. Research, however, found that its support tends to extend only to those who have claims with a high "profitability rate"—a decent shot at a high-damages verdict. This preference is not unique, of course; many law firms also prioritize such cases. Yet this noble "marketing pitch" of litigation funding falls short if people with meritorious claims, but little chance for a large award, do not receive funding due to funders' profit-based concerns.

Frivolous Lawsuits – The same research reported another problem: litigation funding provides unharmed plaintiffs more incentive to make a claim, increasing the number of frivolous lawsuits. From the perspective of the funding company, the more claims that are made, the more profitability a litigation investment can have. Some settlements here and a large verdict

there are enough to justify the endeavor. Defendants in the crosshairs, meanwhile, find themselves scraping their defense reserves to counter fresh waves of lawsuits.

Effects on Jurors – More frequent and well-financed lawsuits can also have indirect effects on jurors. Litigation that assembles a plethora of individual suits (for example, hundreds of suits across the nation over the same product) is sure to attract media attention. Such pretrial publicity—outlining serious, widespread plaintiff claims but offering little in the way of defense responses—can bias potential jurors against that defendant or similar defendants and suggest those claims have merit.

Going beyond this free publicity, litigation funding boosts the signal by supporting paid plaintiff advertisements. Money spent on plaintiff advertising has tripled in the last decade. Far from an accident, blanketing the airwaves is another way third-party funders can fortify their investments. In parading the largest plaintiff wins, advertisements can anchor jurors to higher numbers at trial by providing a point of reference. As jury consultants, we commonly hear jurors cite other verdicts as a factor in their deliberations—e.g., "What's the going rate of lawsuits these days? $50 million for cancer?" or "That one woman got $80 million from Johnson & Johnson, so this is probably worth somewhere around that."

Effects on Plaintiffs – Ironically, funding terms can prey on plaintiffs themselves, a concern expressed by some scholars and lawmakers alike. There is good cause to question whether the injured party ends up with a fair share of their own settlement or verdict. As one New York Assemblyman, William Magnarelli, observed, "Some of the fees being charged by the [funding] companies were so high that whatever the verdict was, the victims ended up getting very little or close to nothing."

Broad data instead suggests that litigation funding serves to redistribute money from those seeking justice into the pockets of wealthy funders. Swiss Re analyst models, for example, indicate that cases involving third-party funding see a notable decrease in plaintiffs' ultimate compensation. The analysts estimated that "plaintiff compensation decreases by 21% relative to the same award in a case without TPLF."

And while lawyers have ethical responsibilities to their clients, funding firms share no such duty. Plaintiffs therefore may be subject to pressure from those paying for their suit. With funders incentivized to hold out for a few large verdicts across a portfolio of cases, it stands to reason that some plaintiffs may be encouraged to pass up terms of resolution that would have been more favorable than the actual outcome.

DEFENDANTS MUST ACT

Given these apparent effects, corporations and the defense bar must coordinate both a long- and short-term response strategy.

Push for Regulation – The cryptocurrency collapse presents merely our most recent example that legislative response to new markets tends to lag—often to ruinous effect. In this case, lawmakers have only sporadically sought to regulate litigation funding; the gates remain wide open to profiteering at the expense of our civil justice system.

Rather than trying to battle the problem in the courtroom, when it is mostly too late, defendants' best strategy will be to preempt its unhindered growth altogether. Businesses must urge legislatures nationwide to impose rules and transparency on litigation funding firms. Among other things, regulations should establish that:

- Settlement decision-making control remains vested with plaintiff(s)
- Funding agreements are conspicuous, in writing, and signed by plaintiff(s)
- Financing amounts are capped
- Fees, charges, and interest rates are capped
- Funding documents are exchanged in discovery
- Guidance is offered on funding's relevance to litigation and admissibility into evidence

Counter the "David v. Goliath" PR Narrative – If there were ever a public relations battle to be waged, this is it. While the plaintiff bar continues to create ads with the semblance of news articles and pay for billboards and TV spots to anchor jurors to sky-high dollar figures, the defense bar could work to lift the veil on the influence of litigation funding. A documentary on a streaming service, an episode on a docuseries such as "Dirty Money," or a TikTok series via legal or journalism influencers could help inform future jurors about the vast potential resources behind plaintiffs going to trial—and those who stand to benefit most from a massive verdict. By countering the perception of "David v. Goliath" in civil lawsuits, jurors may enter the courtroom with a healthier skepticism toward plaintiffs and their well-paid experts.

IN CONCLUSION

It is all too true that high litigation costs are a detriment to one of the founding principles of our civil justice system—that plaintiffs should receive their day in court. But the introduction of third-party interests appears, thus far, to be more curse than cure. What may be a lucrative pursuit for the investors and funding firms stands to be a nuisance to the system, to defendants, and even to the very plaintiffs it purports to help.

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