Litigation Funding Disclosure Should Be Mandatory

By **David Levitt** (August 3, 2023)

David Levitt

It is time for the various committees evaluating proposed rules to mandate disclosure of third-party litigation funding to act.

In May, the Appellate Rules Committee, evaluating a proposed rule to mandate disclosure of third-party litigation funding, deferred consideration of the issue to await further developments from the Civil Rules Committee which, it noted, has studied the issue "for years."[1] The Multidistrict Litigation Subcommittee recently reached a similar conclusion.[2]

In fact, there are compelling reasons to mandate such disclosure, and there is no good reason for further delay. Such disclosure is necessary for the even-handed administration of justice, and to guarantee that defendants, no less than plaintiffs, are able to "secure the just, speedy, and inexpensive determination of every action and proceeding" required by Federal Rules of Civil Procedure, Rule 1.

News reports from Reuters and The New York Times in 2015 and 2018 assert that litigation funders such as MedStar Funding and Law Cash — among others — urged women with vaginal mesh to have unneeded surgery to enhance the value of their claims.[3] In another mesh-related litigation, the law firm AkinMears settled a dispute with its former business development officer who claimed to have secured $93 million in litigation funding for an interest in a portfolio of over 14,000 mesh lawsuits.[4]

Another funder, Litigation Management and Financial Services, placed ads on Craigslist seeking potential plaintiffs to file suit under the Americans with Disabilities Act; eventually, in 2017, the U.S. District Court for the District of New Mexico dismissed 95 "boilerplate lawsuits."[5]

Still another, Legalist, reportedly advertised that it would provide $100,000 in angel funding along with a referral to attorneys for potential plaintiffs filing sexual harassment claims amid the #MeToo movement.[6]

In December 2022, the U.S. Attorney's Office for the Southern District of New York announced the criminal convictions of lawyer George Constantine and Dr. Andrew Dowd, where a litigation funding enabled a $31 million fraudulent scheme in which a litigation funder encouraged and paid for unneeded surgeries for personal injury plaintiffs, resulting in more than 200 fraudulent lawsuits, according to the U.S. Department of Justice.[7]

As discussed in a 2013 article in Plaintiff magazine, medical finance companies and so-called lien doctors sometimes encourage claimants to forgo submitting their medical expenses to their own health insurers or to workers' compensation in order to enhance the amounts of those bills and thereby the overall value of the claim — and some have a network of doctors who seek referrals of such patients, thereby putting their bias and credibility in issue.[8]

These are just a few examples of the ways in which third-party litigation funding potentially affects the actual evidence pending in a lawsuit, and may well be relevant to the issues before the court and jury.[9]

Too often, these issues are given short shrift in the debate over the scope of transparency that should be applied to third-party litigation funding agreements. However, in considering whether to mandate disclosure, and the scope of such disclosure, evaluation of these and other real world examples of the impact of third-party litigation funding on claims — which defendants are required to defend, and courts are required to use scant judicial resources on — should be included.

Among the major arguments against the discoverability of funding agreements are that (1) the funding agreement is irrelevant, and (2) litigation funders have no control over the litigation. As the above examples establish, neither of these is always true — and often are decidedly untrue. Without disclosure of the funding agreement, it is impossible to determine the potential relevance or the degree of control.

As to the irrelevant argument, for over 50 years the Federal Rules of Civil Procedure and the law of most states have mandated that the defendant's litigation funding be disclosed in discovery through production of copies of the defendant's insurance policies that might apply to the claim. The 1970 decision to require such discovery was itself sharply debated, especially because the existence of the defendant's insurance coverage is almost universally inadmissible in the underlying case.

The 1970 Advisory Committee notes are remarkably on point as to the reasons why third-party litigation funding agreements should also be discoverable:

Disclosure of insurance coverage will enable counsel for both sides to make the same realistic appraisal of the case, so that settlement and litigation strategy are based on knowledge and not speculation. It will conduce to settlement and avoid protracted litigation in some cases, though in others it may have an opposite effect.

Even where the funding agreement gives no rights to the third-party litigation funding company to control the litigation and is not otherwise inadmissible in evidence, disclosure permits counsel for both sides to make the same realistic appraisals of settlement and litigation strategy. There is no principled basis for mandating disclosure of insurance coverage but not a third-party litigation funding agreement. And note — the required disclosure of insurance is an actual copy of the insurance policies themselves, not just a description of their existence.

Those who assert that third-party litigation funding does nothing more than "level the field" and ensure that the "fight is fair" miss the point: The field is not level where the plaintiff knows about the defendant's funding but the defendant is left in the dark about the plaintiff's funding.

Every experienced litigator knows of cases where settlements that were otherwise reasonable were scuttled because of a lien that had to be repaid, whether a medical lien, a workers' compensation lien, or others; courts and mediators often require lien holders to participate in settlement conferences as well.

Third-party litigation funders, in essence, hold a lien — especially where the attorneys also sign agreements mandating that they first pay the proceeds of any result to the funding company before paying it to the plaintiff, as is common — according to anecdotal accounts of intra-industry disputes.

And where the funding agreement is with the attorney rather than the party, or where, as is the trend, the attorney is getting funding for a portfolio of cases rather than only the one currently at issue, the need for the defendant, the mediator, or the settlement judge to understand the dynamics of the relationships affecting settlement decisions and strategy is even more heightened.

Further, the very notion that third-party litigation funders have no control over the litigation or its resolution is itself something that the third-party litigation funding industry insists be taken only on faith. How are defendants ever to make a showing of good cause for more discovery — such as set out, for example, in the U.S. District Court for the District of New Jersey rule — if they have no idea what the terms of the funding agreement provide?

Additionally, it is undeniable that the presence of third-party litigation funding, and the need to pay the funder at rates that are sometimes usurious, affects a plaintiff's reasons for not settling at what might otherwise be deemed a reasonable value — regardless of whether such agreements formally qualify as "loans" within the terms of a given state's usury statutes and decisions.

Given the need to pay the third-party litigation funder out of any proceeds, and with the third-party litigation funding company's money already in his or her pocket — if the party rather than attorney was funded — there can often be little incentive for a claimant to settle but instead to roll the dice on even a questionable claim in pursuit of a big score.

Courts have noted this dynamic at work.

In Odell v. Legal Bucks Ltd. Liability Co., a 2008 case where the plaintiff and plaintiff's attorney, after signing the funding agreements, later tried to avoid their payment obligations, the Court of Appeals of North Carolina noted the arguments as follows:

Plaintiff argues that agreements such as the one in this case give litigation lenders a champertous level of control over the borrowers' lawsuits because they have a deleterious effect on the borrowers' abilities to settle their underlying claims. According to Plaintiff, a rational borrower is likely to reject any settlement offer that is less than the amount of the advance and accrued interest she owes to the lender, even if the settlement offer is perfectly reasonable. This is because the borrower will be required to pay her entire recovery to the lender, and will in effect receive nothing from the settlement. Instead, Plaintiff argues, the borrower will bring her claim to trial. If borrower loses at trial or secures a small recovery, she is no worse off than she would have been had she accepted the settlement offer.[10]

Or as the Massachusetts Land Court stated in its 2004 Conlon v. Rosa decision: "Such hidden funding can introduce a dynamic into a plaintiff's case — an agenda unrelated to the merits, a resistance to compromise — that otherwise might not be present and, unless known, cannot be managed or evaluated."[11]

The presence of funding can result in cases going to trial that would otherwise settle, resulting in unnecessary expense and use of resources — for both the court system and the defendants — that ought not have been incurred. That alone is reason for the existence and the terms of such funding to be transparent to all concerned in the litigation.

Even where the third-party litigation funding agreement may not be admissible in evidence, it may nonetheless be relevant to other court determinations.

In product liability, toxic tort, and class action litigation, for example, the plaintiff has little exposure to that expense because it has limited information to be discovered. On the other hand, the discovery requests to the defendants are often massive in scope with little incentive for the plaintiff to narrow the scope unless required to do so by the court. Thus, defendants frequently bear the vast majority of the discovery response cost and risk.

Litigation funders do not tend to invest in small matters where the return on investment is limited. The Federal Rules of Civil Procedure, Rule 26(b)(1), expressly provides that consideration of the parties' resources is one factor to be evaluated as part of the proportionality analysis. In addition to proportionality, Rule 26(c)(1)(B) gives the court discretion to consider the "allocation of expenses" in determining the scope of permissible discovery requests.

Like the insurance disclosure requirement, this dates back to at least the 1970 Amendments to the Federal Rules of Civil Procedure, with the 1970 Advisory Committee notes stating: "[T]he courts have ample power under Rule 26(c) to protect respondent against undue burden or expense, either by restricting discovery or by requiring that the discovering party pay costs."

Courts have held that it is entirely appropriate to shift the cost of responding to the requesting party for burdensome discovery requests. In making that determination, the ability of each party to incur that expense can be an important factor. Hiding the plaintiff's litigation funding inhibits that evaluation.

Further, even an in-camera inspection by the court puts the defendant at a significant and unfair disadvantage, since it is the party that is otherwise exposed to the expense of discovery compliance but would be deprived of the ability to argue the relative abilities of the parties to pay for those compliance costs.

Thus, even where the third-party litigation funding agreement gives the funder no control over the litigation and the funding arrangement is — like insurance coverage — otherwise irrelevant as admissible evidence, discovery of the agreement is nonetheless relevant to other issues that need to be resolved by the court.

Among the arguments made by the third-party litigation funding industry against discoverability, and repeated most recently by the governor of Louisiana in his veto message of a statute that would have required disclosure,[12] is that requiring disclosure would somehow give defendants a litigation advantage into such items as litigation budgets.

Such arguments propose a possible limited form of discovery[13] — as in the District of New Jersey rule or in the opioid litigation — in which the plaintiff need only disclose the existence of funding and an affirmation of lack of control by the funder, but no other details, absent a showing of good cause by the defendant.

Appropriate safeguards about privilege, work product and other concerns about litigation strategy can be handled just as they are when insurers defend cases. With few exceptions — and it is possible that exceptions may arise in the third-party litigation funding setting as well — the attorney's communications with the defendant's insurer, the litigation budget, the insurer's reserves and similar information are outside the scope of discovery — and the same can be true for third-party litigation funding disclosure.

That, however, is entirely different from refusal to produce a copy of the third-party litigation funding agreement itself, just as production of an actual copy of the insurance policy does not itself open up discoverability of the insurer's claims file or the defense attorney's file. If anything, production of the third-party litigation funding agreement evens the playing field.

Even the most field-leveling, non-litigation-controlling, vanilla funding agreement can nonetheless have substantial and important effects on the litigation, court determinations of issues before it, and the overall court system itself.

And where anecdotal evidence — derived mostly from intra-industry disputes that shed light on the terms of the otherwise shrouded funding agreements — suggests that many funding agreements are not merely field-leveling or non-litigation-controlling, the need for transparency is magnified.

Court rules should be adjusted to require that both parties are equally well-informed about the other party's litigation-specific funding. Defendants are already required to disclose theirs. The same principles should apply equally to the plaintiffs side.

David H. Levitt is a partner at Hinshaw & Culbertson LLP. He is chair of the DRI Center for Law and Public Policy's Third-Party Litigation Funding Task Force.

The opinions expressed are those of the author(s) and do not necessarily reflect the views of their employer, its clients, or Portfolio Media Inc., or any of its or their respective affiliates. This article is for general information purposes and is not intended to be and should not be taken as legal advice.

[1] Report of the Advisory Committee on Appellate Rules at 31 (May 11, 2023) available at https://www.uscourts.gov/sites/default/files/2023-06_standing_committee_agenda_book_final_updated_5-30-23_0.pdf (page 100).

[2] Id. at p. 792.

[3] Alison Frankel and Jessica Dye, Special Report: Investors profit by funding surgery for desperate women patients, Reuters, August 18, 2015, available at http://www.abajournal.com/news/article/serial_ada_suits_operated_like_a_carnival_shell_game_depriving_plaintiff_of; Matthew Goldstein and Jessica Silver-Greenberg, How Profiteers Lure Women Into Often-Unneeded Surgery, New York Times, April 14, 2018, available at https://www.nytimes.com/2018/04/14/business/vaginal-mesh-surgery-lawsuits-financing.html

[4] David Yates, Tentative settlement reached in highly publicized AkinMears lawsuit, SE Texas Record, November 11, 2015, available at https://setexasrecord.com/stories/510647677-tentative-settlement-reached-in-highly-publicized-akinmears-lawsuit.

[5] (Carton v. Carroll Ventures, Inc., 2017 U.S. Dist. LEXIS 107135 (D.N.M., July 10, 2017; recommendation adopted, 2017 U.S. Dist. LEXIS 185154 (D.N.M. October 26, 2017)). See, Debra Cassens Weiss, Serial ADA suits operated like 'a carnival shell game,' depriving plaintiff of proceeds, judge says, ABA Journal, July 13, 2017, available at http://www.abajournal.com/news/article/serial_ada_suits_operated_like_a_carnival_shell_game_depriving_plaintiff_of.

[6] Natalie Rodriguez, Going Mainstream: Has Litigation Finance Shed Its Stigma?, Law360,

December 12, 2017, available at https://www.law360.com/articles/992299.

[7] Southern District of New York | New York Attorney And Doctor Convicted Of Defrauding New York City-Area Businesses And Their Insurance Companies Of More Than $31 Million Through Massive Trip-And-Fall Fraud Scheme | United States Department of Justice. https://www.justice.gov/usao-sdny/pr/new-york-attorney-and-doctor-convicted-defrauding-new-york-city-area-businesses-and.

[8] See, e.g., Pebley v. Santa Clara Organics, 22 Cal.App.5th 1266 (Cal.App. 2018), review denied 2018 Cal. LEXIS 5831. ML Healthcare Services, LLC, 881 F.3d 1293 (11th Circ. 2018). See, e.g., Clay Knowles, Rachel Reed and David Glustrom, Medical Funding Companies: A New Problem for an Old Rule, Georgia Defense Lawyers Journal, 2016, available at http://www.wachp.com/wp-content/uploads/2016/06/2016_GDLA_Law_Journal.pdf; Stephen Ellison, Medical Liens: Necessary Evil Or Litigation Advantage?, Plaintiff Magazine, April 2013, available at https://www.plaintiffmagazine.com/item/ medical-liens-necessary-evil-or-litigation-advantage.

[9] More are discussed in the DRI Center for Law and Public Policy's comprehensive white paper on the subject. https://www.dri.org/docs/default-source/dri-white-papers-and-reports/third-party-litigation.pdf.

[10] Odell v. Legal Bucks, LLC, 665 S.E.2d 767, 774 (N.C. App. 2008).

[11] Conlon v. Rosa, 2004 Mass.LCR LEXIS 56, *6 — 8 (Mass. Land Court 2004).

[12] Litigation Finance Disclosure Legislation Vetoed in Louisiana (bloomberglaw.com).

[13] See, e.g., Dai Wai Chin Feman and Will Weisman, November 23, 2022, Litigation Funders Seek Transparency In Disclosure Debate - Law360. Stewart Ackerly, Appellate Funding Disclosure: No Mandate is Right Choice (June 30, 2023), available at https://www.law360.com/articles/1693631/appellate-funding-disclosure-no-mandate-is-right-choice.