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Litigation Funding Slides Downmarket

by Joe G. Hollingsworth and Donald R. McMinn

Through their investments in a lawyer's case(s), litigation funders have fomented economically shaky litigation while making that litigation's resolution more difficult by disguising the settlement decision maker. Now litigation funders are entering a new market—one composed of the plaintiffs themselves, rather than their attorneys. Their new approach is, quite possibly, worse than their initial one.

Web-based platforms speak of creating an ostensible "peer-to-peer" approach by which even individuals can invest in the lawsuits of others. The platforms allow would-be funders to pick and choose lawsuits in which to invest and then direct the investment straight to plaintiffs, not their lawyers. Plaintiffs trade their receipt of funds now in return for agreeing to repay the lender out of any recovery.

In promoting their services, lenders tout that they have no recourse save for their claim on any judgment (a claim that comes after reductions for attorneys' fees and frequently involves a steep interest rate). They proclaim that should the suit fail, they will take nothing. What the lenders do not promote is how, when there is a recovery, their share can swamp the share that actually gets to the plaintiff.

Litigation funders of plaintiffs make the same argument that the lenders to attorneys make—that they are leveling the playing field so that the "big corporations" no longer can discourage individual litigants pursuing small (but valid) claims by drawing out the process beyond the little guys' financial stamina. But, as holds true when these entities fund attorneys, plaintiff-funders' societal-benefit justification does not comport with what defense attorneys see in practice—the practical experience conceded by some who themselves are proponents of third-party litigation funding.

For instance, in a *New York Times* article from 2016, Anthony Sebok, a professor of law at Benjamin N. Cardozo Law School and an advisor to Burford (a litigation funder), can offer only a conditional assertion that "third-party funding of litigation . . . may occasionally help promote justice, or deter future wrongdoing, or bring needed compensation to deserving victims." Anthony Sebok, *Third-Party Litigation Finance Promotes Justice and Deters Wrongdoing*, N.Y. Times, May 26, 2016. Professor Sebok contends that litigation funding should not need to show a benefit to justify its existence. Instead, he argues for a minimal regulatory approach because:

> *People want to do it, and it doesn't hurt anyone—so why not allow it?*

Id. (emphasis added).

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Professor Sebok bases his contention that litigation funding is harmless on his belief that financing does not change the underlying facts to be adjudicated. *Id*.

Professor Sebok's sunny assurances of litigation funding's essential neutrality aside, others do find harm. For the legal profession, there is substantial risk of harm in the creation of litigation settings ripe for conflicts of interest as between the various stake holders. The interest of plaintiffs and funders easily can diverge. This divergence presents a significant problem to counsel, who typically represent the plaintiffs while simultaneously taking instruction from the funders.

The harm to plaintiffs can be financial. Some funders seek out plaintiffs awaiting settlement payments and, in return for cash advances, demand payments that result in inflated returns for the lender. Lenders may argue that consumer banking laws do not apply to these transactions, but the models are being challenged. For instance, in a suit pending against RD Legal Funding, LLC, the New York attorney general and the Consumer Financial Protection Bureau argue that RD Legal engaged in false marketing and "mischaracterize[d] these transactions as 'assignments' [when] they are in fact offers to extend credit or extensions of credit for purposes of the Consumer Financial Protection Act of 2010." *Consumer Financial Protection Bureau, et al. v. RD Legal Funding, LLC, et al.*, Civ. No. 1:17-cv-00890 (S.D.N.Y., Feb. 7, 2017), Complaint, ¶ 6.

The attorney general seeks to void RD Legal's transactions because they are usurious, citing one involving an effective interest rate in excess of 150% annually and alleging that some others ended up with effective annual rates over 250%. Complaint, ¶¶ 7, 25, 29.

The possibility for injury goes beyond the realm of finance; people get hurt. *New York Times* reporters Matthew Goldstein and Jessica Silver-Greenberg exposed a scheme by which funders, working with marketing, surgical, and legal teams, would identify individuals with a medical device (a vaginal mesh implant), convince the individuals that they needed surgery to remove the device, and then loan the individuals the money with which to have the surgery subject to repayment out of an associated product liability claim to be filed by the team lawyer. *How Profiteers Lure Women Into Often-Unneeded Surgery*, N.Y. Times, April 14, 2018. The litigation funders demanded double-digit interest, which they justified by arguing that they needed protection against loss on those cases in which plaintiffs would not secure a recovery.

You know who wasn't protected against loss? The women whose devices were removed. What is striking is that the surgical decision appears to have been made not by the patients' own doctors, but by the lawyers, who had noticed a trend of higher settlements for plaintiffs whose devices had been explanted.

That poor surgical results occurred is not surprising; the women were flown from their home states to selected doctors in Florida and Georgia, where they would have operations in walk-in clinics with surgeons they had never before met and who might not have any of the women's prior medical records. Following the surgeries, some reported complications, the need for subsequent remedial surgeries, and lasting problems, such as incontinence, that left them in an undeniably worse state than they were prior to surgery.

Litigation funding of plaintiffs can carry significant risk of harm. The new breed of litigation funders may wrap themselves in the friendly millennial lingo of crowd-funding and peer-to-peer lending in an effort to market their business model, but as The Who's "Won't Get Fooled Again" taught us back in 1971, "meet the new boss, same as the old boss."