Big-Time Litigation Funding Vs. Consumer Legal Funding

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Last spring, news surfaced that billionaire Peter Thiel had funded Hulk Hogan's lawsuit against Gawker for releasing Hogan's unauthorized sex tape. Since then, the landmark case has had wide-ranging fallout. Gawker filed for bankruptcy after a jury awarded a $140 million settlement in favor of Hogan, and Thiel has moved into an executive position on President-elect Donald Trump's transition team. From a legal and regulatory perspective, the case also provided a unique opportunity to distinguish the varying types of legal finance resources and clear up some misconceptions.

When news of Thiel's involvement broke, it was probably the first time most Americans had heard of third-party litigation funding. Many would probably have been surprised to find out that funding lawsuits in this manner used to be illegal and even now is looked on with great suspicion. The place of litigation funding — essentially an investment in the outcome of a legal claim — in the legal system is much debated in academia, and it doesn't take long to see why.

First, cases like Hogan's could be funded for spite, just to subject the defendant to the significant costs of defending a lawsuit. I know at least one journalist who is understandably nervous that, given Peter Thiel's example, other public personalities with deep pockets could fund lawsuits against reporters who provide negative coverage. Even if unsuccessful, these lawsuits would consume the time and resources of both reporter and employer, chilling free speech and the ability of the press to report honestly. And, journalists are not the only potential victims of this type of harassment; non-journalists who annoy a rich, spiteful individual could also spend a lot of unnecessary time in court. Cases might also be brought to advance some financier's pet project or just for profit.

Second, this type of entrepreneurial financing could facilitate entrepreneurial litigation — pursuit of money rather than pursuit of justice. Trial lawyers are often criticized for being concerned more with profit than the welfare of their clients or society but, at least in principle, professional standards limit them to bringing only cases that are authorized under existing law. As the tobacco litigation of the 80s and 90s showed, however, today's frivolous cases can easily become moneymakers in the future, if you have patience and a lot of money. If truly entrepreneurial litigation ever became the norm, the rule of law could be a thing of the past.

Add in the perceived dangers of increased litigation, with its accompanying clogging of the courts and harm to the economy, and an informed individual should be nervous about where third-party litigation funding is taking us. Those concerns, along with significant pressure by the U.S. Chamber of Commerce on its allies in state legislatures, have led to increasing state regulation of litigation funding.

Unfortunately, these efforts would do little to reduce the real dangers of big-time litigation funding because they are often wrongly focused on another, more benign form of funding. Consumer legal funding seems to be the Chamber's favorite target. But, while its name suggests a connection, the difference between "litigation finance" and "legal funding" is quite important.

Like entrepreneurial litigation funding, consumer legal funding brings in an outsider who provides money to one of the litigants, but there the similarities end. Consumer legal funding provides basic living expenses and/or money for medical bills to poor plaintiffs who already have a lawyer willing to bring the case and the funder gets nothing unless the case is won. That means both the lawyer and the funder have to decide that the case is valid and winnable. The amounts are also typically quite small and the funder has no say in how the case proceeds.

In general, consumer legal funding gives individuals a financial lifeline while they seek a fair and reasonable settlement — usually from an insurance claim after an accident. As a result, consumer legal funding shouldn't increase the danger of cases brought for spite or profit.

As for the general concern that litigation funding will dramatically increase litigation, my own research published in the Loyola University Chicago Law Journal suggests that litigation may increase, but not in the type of volumes that could swamp our judicial system or the economy. With consumer legal funding, the news is even better, since any increase in litigation would likely come from individuals who have actually been harmed but do not have the resources to pay their bills and legal fees. When legitimate claims are brought and justice served, it can actually benefit the economy by deterring bad and inefficient behavior.

Litigation funding, consumer legal funding, and all financial products come with risks that should be considered as states decide whether and how to structure regulations. Two pivotal factors make all the difference in how serious those risks are: intent of the funder, and nature/size of the transaction.

Weight ought to be given to the rights of individuals to enter into voluntary agreements, and legislatures should regulate based on actual risks posed depending on the type of funding. Some groups like the Chamber — usually champions of the free market — have attacked consumer legal funding through overregulation and obscured any differences between big-time litigation funding (like the Gawker case) and consumer legal funding. But mixing these two together is a recipe for bad public policy.

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