NEW YORK UNIVERSITY
JOURNAL OF LAW & BUSINESS

VOLUME 12 SPECIAL ISSUE 2016 NUMBER 3

WHY JUSTICE FOR LITIGATION FINANCIERS IS JUSTICE FOR ALL

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INTRODUCTION

In the October 22nd, 2015 issue, the New York Times Magzine posed a provocative question: "Should you be allowed to invest in a lawsuit?" The question was the headline of an in-depth article that examined the nascent but growing industry of litigation finance, in which investors finance parts of legal cases in hopes of sharing in the eventual settlements.[1] The writer, Mattthas Schwartz, honed in on the question: How does litigation finance impact our justice system? Does it help or hurt it?

Litigation financiers, Schwartz notes, talk about their work as "expanding access to justice" by helping "Davids" fight "Goliaths." But Schwartz concludes differently: "when litigation financiers talk about expanding access to justice and

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1. Mattathias Schwartz, *Should You Be Allowed to Invest in a Lawsuit?*, N.Y. TIMES MAG. (Oct. 22, 2015), http://www.nytimes.com/2015/10/25/magazine/should-you-be-allowed-to-invest-in-a-lawsuit.html?_r=0.

standing up for the little guy, they generally mean helping millionaires pursue claims against billionaires."[2]

Schwartz, it seems, was only exposed to a single slice of the industry, large commercial financings, which likely informed his conclusion. Moreover, his dismissal of the claim that litigation finance promotes justice in a substantive manner reveals a problem that all litigation financiers have to address. The problem is not that litigation finance does not, on the whole, help the "little guy"—it actually does so in many different ways. The problem is that when litigation financiers frame their work broadly as "enacting justice," they often do so primarily as a marketing exercise. Many do not appreciate, and thus struggle at demonstrating, how many of their investments actually help bring about justice for many individuals and organizations. The language of "justice" has been thrown around carelessly and frequently within litigation finance, diluting both its meaning and rhetorical impact. If litigation financiers want outsiders to see the public merits of their work, then they will need to move beyond rhetoric and provide a robust and rigorous explanation of when and how their investments ensure that the civil justice system acts more justly.

To begin, litigation financiers need to establish a meaningful set of criteria for what makes a financing "just" or not. There are, of course, many examples of legal cases in which there is no "little guy," but which still receive financing. For instance, some financiers will fund part of a Fortune 500 company's legal case simply as a maneuver to prevent that company's legal expenses from hitting its P&L statement, not because that company is in need of funds to pursue its case.[3] But there are many other financings that do enable the "little guy" to pursue and obtain the justice that she deserves; those are the examples that this industry should identify, highlight, and celebrate.

The process of defining and celebrating financing's overall positive effect on justice is especially important because regulators and policymakers are increasingly scrutinizing the societal, legal, and moral implications of litigation finance. If

2. *Id.*

3. Jennifer Smith, *Investors Put Up Millions of Dollars to Fund Lawsuits*, WSJ, (April 7, 2013), http://www.wsj.com/articles/SB10001424127887323820304578408794155816934.

policymakers reductively view litigation finance simply as a financial exercise of investors looking for profit, backing millionaires in their legal fights against billionaires, then the entire industry of litigation finance may face a long, uphill battle for legitimacy. But if they view it as a free-market lever that helps bring justice to many people who have been systematically denied access to our legal systems due to a lack of resources,[4] then policymakers will likely ensure that the industry has room not only to persist, but also to grow and thrive.

I.
Litigation Finance: Justice-Oriented Financing

"Litigation finance" is really an umbrella name for dozens of subcategories. The industry's nomenclature is often differentiated by the type of case (e.g. commercial, personal injury, divorce, patent, etc.), by the party receiving the financing (e.g. plaintiffs, defendants, appellants, attorneys, etc.), by the use of proceeds (e.g. attorney fees, litigation costs, living and medical expenses, etc.), and so on.

To introduce more clarity into this complicated and variegated industry, N.Y.U. School of Law's Center for Civil Justice dedicated its 2015 annual conference to the topic of litigation financing. At the conference, speaking as one of twenty-four panelists in a group of industry leaders and academics from around the country, I sought to explain and discuss different subcategories of funding, each of which may raise different conceptual, practical, and/or regulatory concerns.

I proposed that the most meaningful way to have this conversation is to introduce a new criteria: justice. Of course, "justice" is not a new idea within litigation finance, as many financiers claim their investments improve our civil justice system, partly because of their incentives to frame their work as "justice-oriented." But there hasn't been a conversation about what criteria we should use to determine whether a financing is "justice-oriented." That is an essential conversation, one that I hope this paper will catalyze.

Broadly speaking, *justice*-oriented financings allocate and utilize money to enable our civil justice system to be more just.

4. Particularly those who do not have the money to hire an attorney or who cannot hold out for a verdict or fair settlement offer.

It leverages money to equalize the playing field. Everything else is *just* financing.

Which party has the most money should never matter, but it often does. Too often, plaintiffs with meritorious cases receive less-than-fair settlements because they lack the resources to put up a fair fight. Financing can increase these plaintiffs' bargaining power, ensuring that the justice system works as it is intended by enabling them to wait for a fair settlement or their day in court. The logic is simple: If a lack of money is part of the problem, then having access to more of it can be part of the solution.

As Joanna Shepherd, an associate professor at Emory University School of Law, explains, when "third-party financiers invest in cases brought by low-wealth plaintiffs, then the financing may remove cost barriers to justice."[5] Financing becomes "justice-oriented" when it helps the "little guy" utilize money to ensure that the outcome of a case is not determined by which party has more of it.

In determining whether a financing promotes justice, it is more important to examine the facts of a case than to evaluate the intent of the financier. Justice-oriented financing does not always stem from a straightforward desire for justice. After all, financiers may fund the case of a disempowered plaintiff not out of a sense of justice, but simply because they believe the case has a good risk-return profile. Any boon to justice is simply an unintended, "positive side-effect," as financiers ultimately invest "to maximize the expected returns on their investments."[6]

Figuring out whether a financing is "justice-oriented" will require rigorous debate and conversation. I propose that we begin by asking these two questions when examining a financing: is the money being used to finance a plaintiff who has a meritorious case, and is a lack of money a barrier to fighting a fair fight?

Let's look at a few examples:

Peter Thiel, a famous venture capitalist and entrepreneur, recently financed Terry Bollea's (a.k.a. Hulk Hogan) lawsuit against Gawker, a media company. Gawker had published a

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5. Joanna M. Shepherd, *Ideal Versus Reality in Third-Party Litigation Financing*, 8 J.L. ECON. & POL'Y. 593, 599 (2012).

6. *Id.*

sex tape of Bollea, and so Bollea was suing for an invasion of privacy. Thiel, who was outed by Gawker years earlier, invested $10 million in Bollea's legal fight out of what many believe was a personal vendetta against Gawker. Whether Thiel's motivation was "right" or "just" is beside the point. The fact is that Bollea had a meritorious case (the jury decided in favor of him), one that he said, despite being a celebrity, he would not have been able to fully pursue without Thiel's financial help. Thiel's investment is thus an example of justice-oriented financing.

Here is yet another example. TechForward was a startup founded in 2007 by two UCLA business school classmates looking to develop a platform for people to lock in the value of electronics that often depreciate quickly.[7] This once-unique idea of "trading in" electronics was clearly a smart one given its popularity with retailers today, and the retail giant Best Buy recognized the opportunity and engaged in a trial program with TechForward's platform in a number of stores.

Soon enough, Best Buy chose to breach its service agreement by secretly copying TechForward's proprietary analytical model and start its own program based on TechForward's technology.[8] It then proceeded to abruptly terminate its contract with TechForward, betting that TechForward would not have sufficient funds to fight a prolonged legal battle.

Best Buy was correct in that it had an enormous structural advantage. Defendants enjoy what economists call "monopsony power," which is just like monopoly power, except that one buyer has all the market power instead of one seller. Essentially, the defendant is the only legally authorized "buyer" of the plaintiff's liability claim. As Stephen Gillers, one of the most prominent legal ethicists in the United States, explains:

> [The defendant] is under no time pressure. It is, furthermore, the only authorized purchaser of [the plaintiff's] claim, the only one allowed to bid on it. Now it requires no MBA to recognize that if one per-

7. *Interview with Jade Van Doren and Marc Lebovitz, TechForward*, SOCALTECH.COM (Apr. 30, 2007), http://www.socaltech.com/interview_with_jade_van_doren_and_marc_lebovitz_techforward/s-0008839.html.

8. Leena Rao, *TechForward Wins $27M in Lawsuit Against Best Buy Over Stolen Trade Secrets*, TECHCRUNCH (Dec. 5, 2012), https://techcrunch.com/2012/12/05/techforward-wins-27m-in-lawsuit-against-best-buy-over-stolen-trade-secrets/.

> son is under duress and needs to sell something and another person is the only one legally allowed to buy it, the buyer has an enormous advantage.[9]

Best Buy's bet almost paid off—until TechForward's venture capitalists (VCs) stepped in.

NEA and First Round Capital, two of the world's most prominent VCs, were investors in TechForward when the breach occurred. To keep TechForward out of bankruptcy, they poured in roughly $750,000 to finance TechForward's legal case against Best Buy. TechForward's VCs were not trying to be charitable. They were trying to recoup their invested funds, but they also wanted to hold Best Buy accountable. Josh Koppleman, a partner at First Round Capital, explained, "We needed to send a message . . . If big companies believe they can violate agreements with immunity because a startup can't afford to sue them, it is bad news for every startup in the ecosystem."[10] Although they probably would not refer to themselves as such, these two VC firms became litigation financiers the day they made that financing. Two years later, TechForward won a $22 million verdict.

NEA's and First Round Capital's first priority was certainly financial: to keep TechForward out of bankruptcy and to make a profit. But, more to the point, their financing also enabled the little guy to level the playing field. That is justice.

To be clear, in order for financing to act as a "great equalizer," it is not enough for the plaintiff to have less money than the defendant. As Schwartz points out, millionaires do have less money than billionaires, but most millionaires still have plenty of money to ensure that they receive a fair outcome. Just like in political fundraising campaigns, once you pass a certain point, the differences in capital become trivial.[11] In this case, TechForward did not just have less money than Best Buy—it simply did not have enough money, period. And so it

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9. Stephen Gillers, *Waiting for Good Dough: Litigation Funding Comes to Law*, 43 AKRON L. REV. 677, 683 (2010).

10. *Why First Round Capital Funded a Lawsuit,* REDEYE.COM (Dec. 5, 2012), http://redeye.firstround.com/2012/12/why-first-round-capital-funded-a-lawsuit.html.

11. Chris W. Bonneau & Damon M. Cann, *Campaign Spending, Diminishing Marginal Returns, and Campaign Finance Restrictions in Judicial Elections*, 73 J. POL. 1267 (2011).

could not hold Best Buy accountable until it received financing.

What litigation financing does for plaintiffs is introduce a threat to defendant's monopsony power: competition. Instead of being stuck with the defendant as the sole buyer, TechForward was able to sell equity of its company (where the only asset was its lawsuit) to financiers and access critical liquidity, empowering TechForward to make decisions free from duress. Instead of being bullied into a cheap settlement by a deep-pocketed defendant, TechForward was able to fight vigorously for a fair resolution.

One can find many similar examples of how litigation financing promotes justice across all of its traditional subcategories. Most subcategories will have a mix of justice-oriented financings and regular financings; having robust criteria for what "justice" looks like can help us sift through all the financings and highlight the ones that promote justice. But there is one subcategory in which virtually every financing is justice-oriented: personal injury.

II.
Justice-Oriented Financing: Personal Injury

Personal injury financing is the subcategory most systematically oriented towards justice. In virtually every case, the plaintiff is the "little guy" going up against a powerful defendant.

Compared to most other plaintiffs, personal injury plaintiffs are more likely to lack the financial resources to fight a fair fight. That is because an unexpected accident can often have far-reaching consequences for the injured beyond the injury itself. It can put a person out of work and bury her or him under a growing pile of medical, living, and other expenses. In the United States, many lawsuits take years to resolve. So if a plaintiff is one of the seventy-six percent of Americans who are living paycheck to paycheck, the years of waiting for a resolution may be worse than the accident itself.[12] Most plaintiffs are not trying to turn their injuries into a get-rich-quick scheme, but rather trying to get through the worst days of their lives.

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12. Angela Johnson, *76% of Americans Are Living Paycheck-to-Paycheck*, CNN.com (June 24, 2013), http://money.cnn.com/2013/06/24/pf/emergency-savings/.

In personal injury cases, injured victims are not usually facing the party that harmed them, but large insurance companies who are standing in on behalf of the offenders as "professional defendants." Insurance companies are well-aware that plaintiffs lack the funds not just to last a long legal battle, but to cover their basic living expenses. Thus insurers often prolong the legal process, waging a war of attrition that effectively compels plaintiffs to accept quick, less-than-fair settlements. It is a blatant injustice that happens daily, even in the most clear-cut cases. It is called "frivolous defense," a phrase you will have heard much less frequently than "frivolous lawsuits," even though many scholars believe it is the former that causes our courts to clog, rather than the latter. Richard L. Abel, Cornell professor of Law at UCLA, notes in an article in the New York Law School Law Review that the real crisis in tort litigation is "defendants who assert frivolous defenses, abuse procedure, file hopeless appeals . . . all to discourage legitimate claims and delay payment."[13]

Best Buy is a behemoth, but its primary business is selling electronics; like most defendants in commercial litigation suits, it only engages in lawsuits once in a while. Insurance companies, on the other hand, make their living trying to figure out how to minimize payouts—a report released by the Consumer Federation of America details the various ways in which insurance companies adjust computerized systems to make sweeping, "lowball" claims to injured consumers.[14]

Not only do insurers bring the best legal experts and resources to the table, but they also have invested millions upon millions of dollars in long-term strategies such as PR campaigns and congressional lobbying to tilt the system in their favor. Just last year, The National Association of Mutual Insurance Companies awarded State Legislature of the Year Awards to three legislators who made personal injury plaintiff financing less accessible to consumers in Tennessee. Insurers are not just good at the litigation game; they help write the rules. In

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13. Richard L. Abel, *How the Plaintiffs' Bar Bars Plaintiffs*, 51 N.Y. L. SCH. L. REV. 345, 348 (2006–2007).

14. Mark Romano & J. Robert Hunter, *Low Ball: An Insider's Look at How Some Insurers Can Manipulate Computerized Systems to Broadly Underpay Injury Claims*, CONSUMER FEDERATION OF AMERICA (June 4, 2012), http://www.consumerfed.org/pdfs/Studies.ComputerClaims06-04-12.pdf.

the personal injury market, defendants are systematically favored over plaintiffs.

When we talk about "expanding access to justice," we typically mean ensuring that people have attorneys. But that definition is incomplete. While many PI plaintiffs have contingency attorneys, they still may not have equal access to justice if they cannot afford to wait for a fair settlement or for their day in court. Delayed justice is no justice at all.

To be clear, insurance companies do serve a legitimate and valuable purpose. Liability insurers rightly protect defendants from financial catastrophe due to a single mistake, and plaintiffs need a similar kind of protection. Litigation financing for plaintiffs meets that need, as it is the mirror equivalent of what defendants receive through their liability insurance. As Professor Charles Silver at University of Texas Law School argues, just as liability insurance shifts liability to insurers, plaintiff financing can shift the bulk of a plaintiff's expenses, such as medical bills and living expenses, to financiers, enabling plaintiffs to get their full and just compensation.[15]

Despite their equivalence, today the PI market suffers from a certain "ick factor," as the idea of financing PI lawsuits offends many people's sensibilities. The great irony is that when liability insurance first came on the market in the 1800's, it too was considered repugnant and dangerous.[16] People believed that abdicating responsibility to a third party would incentivize recklessness, increase accidents, and distort the legal system by introducing a non-party into the proceedings. Fast-forward a century and this free market solution has become so successful that car insurance is legally required in almost every state.

It is clear that there is a dire and vast need for litigation financing in the personal injury market. Not only does the personal injury market suffer from a greater systemic bias than any other litigation finance market, but also the stakes are often far higher. PI plaintiffs are fighting not for the health of

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15. Charles Silver, *Litigation Funding Versus Liability Insurance: What's the Difference?*, 63 DEPAUL L. REV. 617.

16. *New York Roundtable Interview with Professor Charles Silver on Litigation Funding and Liability Insurance,* BENTHAM IMF (May 16, 2014), http://www.benthamimf.com/blog/blog-full-post/bentham-imf-blog/2014/05/16/new-york-roundtable-interview-with-professor-charles-silver-on-litigation-funding-and-liability-insurance.

their businesses, but for their livelihoods and physical recovery—there is no line of defense between them and their injury. The scale and reach of the PI market are far greater as well. Burford, a publicly traded company that finances corporate litigation, has originated almost one hundred financings over its first seven years of existence.[17] A typical PI financing company will likely do more than one hundred financings in a month. According to the National Highway Traffic Safety Administration, car crashes caused over 3.8 million injuries in 2013.[18] And that is just one type of accident that can trigger a PI lawsuit.

Yet, the PI market is still one that is at best, ignored, and at worst, derided, especially in comparison to its sexier, brainier, and more interesting commercial counterparts. Admittedly, some of the criticisms of the PI market are well-deserved. Some of its early actors have acted more like predators than rescuers. And since it appeals to the masses, it employs tactics such as late-night TV infomercials, opening up the entire market to ridicule. But when done correctly, personal injury financing has far greater potential to help bring about justice for millions of ordinary people who could not otherwise afford it.

III.
The Way Forward

Litigation finance is at a critical juncture; in the next few years, the brand and reputation of the entire industry will be determined and solidified. Will litigation finance be tagged as yet another exotic financial transaction, or will it be hailed as a way of correcting some of the systemic inequities in our civil justice system?

"Justice" is the banner that many litigation financiers are waving, and rightly so—the reality is that many financings play a significant role in ensuring that the civil justice system acts the way that it is intended. But litigation financiers need to

17. *FAQs*, Burford Capital, http://www.burfordcapital.com/faqs/ (last visited Dec. 13, 2015).

18. Richard Reed, *Estimated 35,200 US Traffic Deaths Reported in 2013*, Christian Sci. Monitor (Feb. 14, 2014), http://www.csmonitor.com/Business/In-Gear/2014/0215/Estimated-35-200-US-traffic-deaths-reported-in-2013.

develop a more robust understanding of when and how their financings promote justice; if not, the language of "justice" will be seen as mere marketing rhetoric.

For a shared definition of justice to develop, litigation financiers must step out of their silos, which are defined by rather pointless and meaningless subcategories. They must recognize that what unites them is also what makes their industry so special: the power of litigation finance to dramatically and positively help people during what can be the worst days of their lives.

"To name something is to own it," Thomas Friedman of the New York Times once wrote. Right now, the industry is being named by others. It is on litigation financiers to come together, clearly define, understand, and show—meaningfully, not just rhetorically—the substantive impact that financing can have on justice. Only then can litigation finance be defined not by its cynical critics, but by its great social promise.