Congressional Research Service
Informing the legislative debate since 1914

Legal Sidebar

Following the Money: Should Federal Law Require Litigants to Disclose Litigation Funding Agreements?

May 31, 2018

On May 10, 2018, several Members of the 115th Congress introduced the Litigation Funding Transparency Act of 2018 (S. 2815) (the Act), which would require litigants in certain types of cases to disclose whether any commercial enterprise has a contingent right to receive payment in the event that litigant ultimately obtains monetary relief in the lawsuit. The Act is the latest development in an ongoing debate over whether federal law should mandate disclosure of third-party litigation funding agreements—and, if so, to whom and under what circumstances.

This Sidebar analyzes the Act and its significance to federal litigation. After providing a brief overview of litigation funding generally, the Sidebar discusses the ongoing debate over whether federal law should require litigants to disclose litigation funding agreements to their opponents and/or to the court. The Sidebar concludes by describing the relevant provisions of the Act, as well as provisions of another bill currently pending before the 115th Congress that would likewise impose similar disclosure requirements.

Background on Litigation Funding

Third-party litigation funding, also known as litigation finance, occurs when a third party—rather than the parties themselves, their insurers, or their counsel—agrees to cover some or all of the costs of a litigant's lawsuit. In exchange, the litigant agrees to pay that third party a percentage of any settlement the parties ultimately negotiate in the case, or of any judgment the court ultimately awards against the opposing party.

As litigation funding has become increasingly prevalent in the United States in recent years, commentators have debated whether the practice is socially desirable. Supporters of such arrangements, emphasizing that some litigants lack the economic resources necessary to adequately pursue a meritorious claim, argue that litigation funding ensures that injured parties can "bring legitimate claims that otherwise might not be brought." Proponents further contend that, "by putting plaintiffs on 'more equal financial footing against deep-pocketed defendants,'" litigation funding reduces the likelihood that economic difficulties will force litigants to accept suboptimal settlement offers. Opponents, however, maintain that

Congressional Research Service
https://crsreports.congress.gov
LSB10145

the ready availability of litigation funding undesirably increases the volume and length of litigation by incentivizing litigants to initiate and prolong lawsuits even where doing so would otherwise not be economically rational. According to critics, the "prolonged litigation" engendered by litigation funding "hurts defendants, who are forced to divert additional time and money from productive activity to defending litigation."

In addition to disagreeing over whether litigation funding is socially beneficial, proponents and opponents of litigation funding also disagree regarding the extent to which litigation funding agreements create unacceptable conflicts of interest between attorneys, their clients, and third-party funders. Critics of litigation funding argue that, because the third-party funder holds the purse strings to the litigation, the funder may exert control over a party's litigation strategy in ways that are not in that party's best interests. Critics similarly assert that "when funders are fronting the fees for the claimants' lawyers," those lawyers will be motivated to place the funder's interests ahead of those of their clients. Proponents of litigation funding, by contrast, maintain that litigation funding arrangements do not pose any greater risk of ethical conflicts than other capital arrangements that critics of litigation funding find unobjectionable, such as when banks hold security interests in law firms' fee receivables. Amidst this debate, some federal courts have begun scrutinizing litigation financing agreements to assess whether they create improper conflicts of interest, and a few federal courts have required parties to disclose litigation funding agreements to their opponents.

Should Federal Law Require Litigants to Disclose Litigation Funding Agreements?

Litigants generally try to keep litigation funding arrangements secret from their opponents. After all, if a party knows whether its opponent was receiving third-party litigation funding—and, if so, how much—that party would then have an insight into the size of its adversary's litigation budget. In turn, that knowledge could conceivably provide that party a tactical advantage in settlement negotiations and other aspects of the litigation.

Although, as noted above, some federal courts have required parties to disclose litigation funding agreements to the court itself to enable the court to examine whether conflicts of interest exist, federal courts have only rarely required litigants to disclose litigation funding agreements to their opponents. Thus, although some states have enacted laws requiring parties to disclose litigation funding agreements to their opponents, federal law presently imposes no systematic requirement that litigants divulge their financing arrangements to their adversaries.

Commentators have accordingly debated whether federal law should require litigants to disclose third-party litigation funding agreements—and, if so, when and to whom. Some commentators—as well as several Members of Congress—have advocated requiring attorneys to disclose litigation funding agreements to the court and to all parties at the outset of the case so that the court may take appropriate steps to protect the client's interests by monitoring the funder's potential influence over the case. Those who oppose the mandatory disclosure of litigation funding arrangements, by contrast, argue that automatic disclosure requirements would give opposing parties an unfair advantage by exposing their adversaries' litigation budgets. Opponents further contend that requiring parties to disclose litigation funding agreements would embroil courts and litigants alike in costly and time-consuming discovery disputes.

The Litigation Funding Transparency Act of 2018

In response to this debate, several Members of Congress introduced the Litigation Funding Transparency Act of 2018 (S. 2815) (the Act) on May 10, 2018. The Act, which would apply in class action cases and multidistrict litigation, would require litigants to:

- disclose in writing to the court and all other parties the identity of any commercial enterprise that has a right to receive payment that is contingent on the receipt of monetary relief in the action by settlement, judgment, or otherwise; and
- produce agreement creating such a contingent right for inspection and copying.

The Act's sponsors maintain that the Act "will shed light on third party litigation financing agreements to ensure that the court and opposing parties are made aware of who is financing the litigation and whether or not there are any conflicts of interest." Opponents of the Act, by contrast, contend that "requiring plaintiffs to disclose their sensitive financial arrangements to defendants" will "create expensive and time-wasting frolics and detours in litigation" and will be misused "as a tactical device by defendants." The Act is presently pending before the Senate Committee on the Judiciary.

Other Pending Legislation

The Act is not the only bill pending in the 115th Congress that would mandate disclosure of litigation funding agreements. The Fairness in Class Action Litigation and Furthering Asbestos Claim Transparency Act of 2017 (H.R. 985) (FICALA) would similarly require plaintiffs' attorneys in class action cases to "promptly disclose in writing to the court and all other parties the identity of any person or entity, other than a class member or class counsel of record, who has a contingent right to receive compensation from any settlement, judgment, or other relief obtained in the action." As of the time of this writing, FICALA has passed the House and is pending in the Senate.

Non-Legislative Options

Congress is not the only entity that possesses authority to alter the rules governing the disclosure of litigation funding agreements. A few federal courts have issued standing orders mandating the disclosure of litigation funding arrangements in certain types of cases, and the Advisory Committee on Rules of Civil Procedure has also considered whether to modify the Federal Rules of Civil Procedure to require such disclosures. As noted above, however, at present there is no nationwide requirement that would uniformly mandate disclosure of litigation funding agreements in federal litigation.

Author Information

Kevin M. Lewis
Legislative Attorney

Disclaimer