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TRIAL BY SOCIAL-MEDIA: THE RISE OF LITIGATION CROWDFUNDING

Michael Elliott

I. INTRODUCTION

Crowdfunding is a rapidly growing means of raising capital and fund new ventures through small individual contributions. In just a few years, this online industry has grown into an effective means of funding everything from art projects to consumer goods to business startups. Crowdfunding websites like Kickstarter, Indiegogo, and AngelList have taken off, raising $2.7 billion in 2012 and $5.1 billion in 2013. The industry is expected to continue growing at a rapidly accelerating rate. While most crowdfunded projects offer simple rewards for contributors—early access to funded products, special recognition for contributions, or opportunities to meet the project’s developers—a new development in crowdfunding will allow investors the chance to become a shareholder in the company, bringing the industry closer to traditional investment methods.

Like crowdfunding, litigation financing is a relatively new and rapidly growing industry. The practice involves providing loans to plaintiffs who need funding for relatively high-value lawsuits in exchange for large payouts upon the success or settlement of the case. Litigation financing has long been a controversial topic. The legality of litigation financing has been challenged on numerous occasions with compelling arguments both for and against the practice. Despite the controversy, litigation financing is becoming

5. MASSOLUTION.COM, supra note 3.
8. Id.
9. Id.
10. See Susan Lorde Martin, Litigation Financing: Another Subprime Industry That Has A Place

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an accepted part of a rapidly evolving legal world and attracts more and more investors every year. While currently a fairly small market, reports of firms with annual returns of fifty percent or more per year make it a lucrative option for savvy investors.

Seeking to capitalize on the growing popularity of both crowdfunding and litigation financing, a group of entrepreneurs created LexShares. Launching in November of 2014, LexShares offers investors a chance to bet on the outcomes of commercial legal disputes and boasts an average rate of return of more than fifty percent. To assure these returns, LexShares vets any cases before listing them on its website. LexShares earns a percentage of each investment before any litigation and the rest is sent to plaintiffs to litigate their cases. The overall design of LexShares website mirrors that of popular crowdfunding websites like Kickstarter.

Funded Justice, another litigation financing website, offers an entirely different model of litigation finance. Launched in December of 2014, the website relies entirely on donors who receive no compensation for their contribution. Designed to help those who cannot afford basic legal services, the website offers cases in over a dozen areas of law, including family law, criminal law, consumer transaction law, and employment law. In exchange for its services, Funded Justice collects a fee from each campaign. LexShares and Funded Justice show the breadth of litigation financing companies operating today.

Part II of this comment provides a detailed overview of litigation in the United States Market, 53 VILL. L. REV. 83 (2008).


15. Fisher, supra note 11.

16. Id.


20. Graham, supra note 18.
financing and crowdfunding, and outlines the most common arguments for and against litigation financing. Part III examines current case law concerning litigation financing, including the various legal strategies aimed at defeating the practice. Part IV argues that both LexShares and Funded Justice create dangerous precedents. Unlike standard litigation financing, which is relatively innocuous, crowdfunded litigation financing poses major risks and could encourage frivolous lawsuits. These risks must be carefully remedied through regulation.

II. BRIEF HISTORIES OF CROWDFUNDING AND LITIGATION FINANCING

A. Crowdfunding

“Crowdfunding” is the effort to fund ventures, “by drawing on relatively small contributions from a relatively large number of individuals using the Internet, without standard intermediaries,”21 and is a relatively new fundraising source in the United States.22 ArtistShare, the first major crowdfunding platform, launched in 2003.23 The website allowed musicians to seek donations to produce digital recordings.24 The platform’s first crowdfunding campaign raised $130,000.25 Inspired by ArtistShare’s success, more crowdfunding platforms emerged, the most successful of which are Indiegogo, started in 2008, and Kickstarter, which began in 2009.26 To date, Kickstarter has raised over $1.9 billion for crowdfunding projects.27

Crowdfunding is used to fund many ventures, including new consumer products, art projects, humanitarian projects, and films.28 Traditionally, crowdfunding ventures seek to raise small amounts of capital for one-time projects.29 Unlike a traditional investor who receives a return and increase of their capital, crowdfund investors generally receive some nominal reward in exchange for their

22. See Freedman & Nutting, supra note 1.
23. Id.
24. Id.
25. Id.
26. Id.
29. Mollick, supra note 21, at 3.
money. Increasingly, however, entrepreneurs are turning to crowdfunding as a source of equity for new business ventures.

This process was aided by the passage of the Jump Start Our Business Startup Act (JOBS Act) in 2012, though the regulations that had the most significant impact on crowdfunding were not fully enacted by the SEC until March of 2015. The law, once fully enacted, will allow for crowdfunding of equity interests in startup companies. Before the JOBS Act, equity crowdfunding was unavailable for these businesses “because it involved the sale of securities,” which generally must be registered with the SEC. The new rules provide an exemption from this registration requirement, and will enable smaller companies to offer up to $50 million in securities during a twelve month period while protecting investors through certain “eligibility, disclosure, and reporting requirements.” The result is a more friendly approach towards equity crowdfunding, one of the four main types of crowdfunding models.

Crowdfunded projects generally fall under one of four fundraising models. Many crowdfunded efforts are based on a patronage model, where funding is treated as a donation with no expected returns. However, the most prevalent crowdfunding model is the reward-based model. These rewards depend upon the level of contribution, with higher-quality rewards for larger pledge amounts. Crowdfunding rewards range from special thank you messages from the project team to roles in film projects. Another crowdfunding approach is the lending model, in which funds raised are treated as a

30. Id.
31. Id.
33. Mollick, supra note 21, at 3.
35. See Sec. & Exchange Comm’n, supra note 32.
37. Mollick, supra note 21, at 3.
38. Id.
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 loan. Under this model, backers are entitled to a return on their investment. This model, also known as “peer-to-peer” or “marketplace” lending, emerged in 2006 as a welcome alternative to bank loans, which have become more difficult to obtain since the 2008 financial crisis. Debt-based crowdfunding platforms such as Lending Club, a San Francisco business, vet potential borrowers much like a traditional lending institution. The final model is equity crowdfunding. As mentioned previously, equity crowdfunding has only recently become feasible in the United States and is rare worldwide.

B. Litigation Financing

Like crowdfunding, litigation financing, or litigation funding, utilized the Internet to grow into a full-fledged industry. Unlike crowdfunding, litigation funding has remained a relatively small industry, having tapped into only roughly $1 billion of the estimated $200 billion U.S. litigation market. Additionally, unlike crowdfunding, litigation funding has received relatively little attention from the general public and even less support.

Litigation financing firms provide non-recourse loans to individuals engaged as plaintiffs in lawsuits. These funds may be used “to cover personal [or] legal expenses while pursuing litigation.” If the plaintiff wins or settles the case, the firm is entitled to a share of the proceeds, plus interest. If the plaintiff loses the case, “nothing is repaid and the lender loses the money

41. Mollick, supra note 21, at 3.
42. Id.
43. Freedman & Nutting, supra note 1.
44. See id.
45. Mollick, supra note 21, at 3.
46. Equity crowdfunding makes up less than five percent of all crowdfunding investment worldwide. Id.
47. Martin, supra note 10, at 83.
49. A non-recourse loan is “a loan in which the lender has the right to take only the asset bought with the loan if it is not paid back, and does not have the right to take any other assets. Non-Recourse Loan, CAMBRIDGE DICTIONARIES ONLINE, http://dictionary.cambridge.org/us/dictionary/business-english/non-recourse (last visited Mar. 30, 2015).
50. Martin, supra note 10, at 86.
52. Id.
For this reason, litigation financing firms must carefully vet each potential investment. Firm members must have both sound legal sense and business savvy to turn a profit. If litigation is successful, however, firms stand to make large returns on their investments. For example, in 2011, Burford Capital, one of the largest litigation investment firms, made $32 million on nine cases for a return of ninety-one percent.

The practice of litigation financing emerged in the late 1980s and early 1990s and primarily involved corporate lawsuits. More recently, however, litigation financing has expanded beyond corporate lawsuits into areas including personal injury, patent law, and employment discrimination cases. Much of the controversy surrounding litigation financing arose when litigation financing firms began to offer funding for these individual plaintiffs. Because these plaintiffs are generally poor individuals unable to hire their own attorneys, many viewed the high interest fees charged by litigation finance companies as predatory. Interest rates in personal injury suits have been known to rise as high as 280%. These huge fees tended to shift focus toward the litigation financing firms and away from the defendants of the case, resulting in large corporations and their insurers supported this shift. These types of defendants were more than happy to see the public's ire on another party. On the other hand, those in support of litigation financing argued that litigation financing is often the only source of funding for plaintiffs who otherwise cannot afford the cost of litigation.

In addition to concerns for the underprivileged plaintiff, there are a number of ethical issues involved with the practice of litigation financing. Among these are concerns that litigation financing "can inappropriately influence cases." The United States Chamber of Commerce has argued that the presence of third party investors can

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53. Martin, supra note 10, at 86.
54. Alden, supra note 7.
55. Id.
56. Id.
57. Id.
58. Dietsch, supra note 51, at 693.
59. Id.
60. Martin, supra note 10, at 84.
61. Id.
63. Martin, supra note 10, at 84.
64. Id. at 84-85.
65. Alden, supra note 7.
affect a plaintiff’s legal strategy. Additionally, others argue that litigation financing effectively turns the legal system into a stock market. Finally, many argue that the practice might encourage frivolous lawsuits.

Despite these concerns, the litigation financing industry continues to grow. As the practice gains acceptance, many lawmakers seek to regulate the industry, rather than ban it outright. Several groups are pushing for rules that require transparency about cases funded through litigation financing, and in New Jersey, lawmakers are considering a bill that would cap interest rates on litigation loans. The most stringent litigation financing regulations apply at the individual plaintiff level, while corporate litigation remains largely unregulated. To date, there are no government organizations with direct oversight over litigation financing firms.

C. LexShares and Funded Justice

Launched on November 11, 2014, LexShares was the first litigation financing company to apply the crowdfunding method to litigation financing. LexShares was co-founded by Jay Greenburg, an investment advisor who previously worked with Deutsche Bank, and Max Volsky, a veteran in the litigation finance industry and a practicing attorney at Schmidt, Volsky & Perle, a New York law firm. The company applies the lending model of crowdfunding, and accepts funds only from those individuals who are "accredited investors" under SEC regulations. For an individual to be an accredited investor, they must have an earned income exceeding $200,000, $300,000 jointly for a married couple, for the prior two years or have a net worth of more than $1 million, excluding the value of their primary residence. Finally, while investors in

66. Id.
67. Id.
68. Id.
69. Id.
71. Id.
72. Fisher, supra note 11.
73. Hashway, supra note 62, at 751.
74. Weiss, supra note 17.
75. LEXSHARES, supra note 14.
76. Weiss, supra note 17.
77. Id. The SEC defines several classes of accredited investor, most of which apply to legal entities other than natural persons. 17 C.F.R. § 230.501. The above examples are the only classes of
LexShares’ crowdfunded lawsuits earn money only if the plaintiff wins, LexShares earns its profits, win or lose, by receiving a portion of the total funds raised by the plaintiff. LexShares did not have a problem acquiring funding for its first case, a products liability suit. In a press release, Greenburg, Lexshares’ CEO, stated that this first offering, $250,000 for a product liability suit, was “wildly oversubscribed.” LexShares’ current lawsuits include a whistleblower lawsuit, a breach of contract claim against an oil and gas developer, and products liability claims.

Launched just one month after LexShares, Funded Justice seeks to provide funding for low-income plaintiffs who cannot afford to hire an attorney on their own. The project, founded by Chicago attorney Michael Helfand, utilizes the patronage model. Unlike LexShares, Funded Justice does not require investors to be accredited. The website earns money by collecting a five percent fee from its campaigns. The cases currently listed on the Funded Justice website include a landlord tenant lawsuit, child custody disputes, and a class action lawsuit. Within four months of its creation, two cases realized their fundraising goals, and Funded Justice successfully raised more than $4,000 for plaintiffs seeking representation.

III. CASE LAW CHALLENGING LITIGATION FINANCING

Sometimes funded litigants, after securing a favorable outcome in their case, will attempt to invalidate the financing agreement to avoid repayment. In these cases, a number of arguments can be advanced to support requiring repayment. The most common of these are

78. Id.
79. Id.
80. Id.
85. Graham, supra note 18.
87. Id.
88. See infra Subparts III.A-III.C. This repayment avoidance applies only to LexShares as Funded Justice does not seek any repayment for its donations.
claims of usury, maintenance, champerty, and barratry. A usury claim alleges that the litigation financing arrangement was a loan with an unlawfully high rate of interest, while maintenance, champerty, and barratry focus on the undue influence the arrangement may have on the outcome of a case. Another argument plaintiffs may use in seeking to void agreements is a claim the arrangement was against public policy. Finally, in at least one case, a court has found litigation financing agreements to be a form of gambling.

A. Usury

One of the most common defenses against a litigation financing agreement is a claim brought under usury laws. Black's Law Dictionary defines usury as "the charging of an illegal rate of interest as a condition to lending money." Modern usury legislation protects borrowers from unreasonably high interest rates. Most states have statutes setting limits on interest rates, though the limits vary from state to state. At a minimum, usury laws bar the lender from recovery of any interest if the interest rate is found to violate the usury laws. In some jurisdictions, the borrower may recover penalties for usury violations. Some jurisdictions declare usurious agreements unenforceable entirely, depriving the lender of both the interest as well as the principal. Usury laws do not apply to advances, in which a lender loans money to a borrower, the repayment of which is subject to a contingency. As previously noted, repayment in litigation financing agreements is generally contingent upon plaintiffs winning their cases. This means that,
ordinarily, such arrangements are not subject to usury laws. Courts have ruled consistently with this conclusion.

_Aldrich v. Aldrich_ is one of the earliest cases challenging a litigation financing agreement. Charles Aldrich, a practicing attorney, represented the L.P. Larson, Jr. Company in two litigation proceedings. In need of money, Aldrich borrowed $20,000 from Charles Brown, a friend and fellow attorney. In return, Aldrich agreed to repay the $20,000 plus ten percent interest on his contingency fee in the proceedings “in the event of a payment or settlement for more than $1,590,000.” The agreement stated that the lender would realize not less than $50,000 from this interest.

Ultimately the litigation was settled for $1,900,000 in favor of Aldrich’s client. The $603,333 contingency fee due to Aldrich, now deceased, was paid to his trust. Brown claimed that he was entitled to the $20,000 he had loaned Aldrich, with interest, plus ten percent of the contingency fee, approximately $60,333. Aldrich’s trustee claimed that the arrangement between Aldrich and Brown was usurious and sought to void the agreement. To ensure that the agreement was considered a loan, rather than an advance (to which usury laws do not apply), the trustee read the agreement as imposing an absolute obligation to pay Brown both the $20,000 he loaned to Aldrich as well as an additional $50,000. This would mean that Brown would receive at least $70,000 under the terms of the agreement.

In rejecting all claims that the litigation financing agreement was usurious, the Illinois Court of Appeals determined that the agreement hinged on a contingency and was not a loan. The agreement stated repayment of the $20,000 occurred “when payment or settlement is made.” As “[f]ew things in this world are more uncertain and
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dubious than the result of a lawsuit” and this uncertainty cannot be removed, the court viewed the agreement as contingent on the lawsuit.117 The court also determined that the provision granting Brown at least $50,000 was a contingency hinging on the outcome of Aldrich’s case.118 The court concluded its analysis by noting that Brown was entitled to the full amount of the repayment as “Brown was risking every dollar he advanced to Aldrich and [ ] his only hope of getting any of it back was based alone upon the contingencies [ ] that [Aldrich’s client] should win the law suit, and, second, that the decree entered would be for an amount large enough to cover prior encumbrances as well as Brown’s claim.”119

Courts are not always willing to uphold litigation financing agreements, however. In cases where the “contingency” is illusory and repayment is virtually guaranteed, courts are more willing to declare the financing agreement usurious. In Lawsuit Financial, L.L.C. v. Curry, the defendant, Mary Curry, was injured in an automobile accident and brought suit against the party responsible for her accident.120 During its pleadings in advance of the trial, the defendants in Curry’s lawsuit admitted liability, and disputed only the amount of damages owed.121 While still in the early phases of the accident lawsuit, she approached Lawsuit Financial, L.L.C. for advance funds and received a total of $177,500 in three separate payments.122 In return, Curry agreed that she would repay the loan with the greater of $887,500 or ten percent of the proceeds of the lawsuit.123 The first advance was not made until nine days after the jury verdict awarded Curry $27 million in damages.124 Ultimately, the suit would settle for $4.7 million.125 Lawsuit Financial demanded that Curry pay the $887,500 owed.126 After being repeatedly ignored, Lawsuit Financial sued Curry and her lawyer for conversion, breach of contract, and tortious interference with the contract.127

The Court of Appeals ruled that the agreement was usurious.128

117. Id. at 358.
118. Id.
119. Id. at 365.
121. Id.
122. Id.
123. Id.
124. Id. at 239. The only remaining issues “were a motion for remittitur and a determination of the propriety of the” jury award. Id. at 237.
125. Lawsuit Fin., 683 N.W.2d at 237.
126. Id.
127. Id. at 235.
128. Id. at 240.
Due to the timing of the advance and the prior admission of liability, the court ruled that the plaintiff had an "absolute right to payment" and deemed the agreement to be a loan.\textsuperscript{129} As the interest rate on the loan far exceeded the maximum legal interest rate of seven percent, Lawsuit Financial was barred from recovering any interest or other fees.\textsuperscript{130}

Further, in cases where there was a very low probability that judgment would not be in favor of the borrower and repayment was virtually guaranteed, at least one court has been willing to declare such financing agreements to be usurious.\textsuperscript{131} In \textit{Echeverria v. Estate of Lindner}, the borrower was injured in a construction accident.\textsuperscript{132} The debtor entered into an agreement with LawCash and was given "$25,000 at an interest rate of 3.85\%, compounded monthly."\textsuperscript{133} The court held that, given the high probability that the plaintiff would win his strict-liability labor law case, the transaction was a usurious loan.\textsuperscript{134} The court subsequently adjusted the agreement's interest rate to sixteen percent interest per annum.\textsuperscript{135}

\textbf{B. Maintenance, Champerty, and Barratry}

Maintenance, champerty, and barratry are three similar common law doctrines arising out of English common law and can be traced back to medieval England.\textsuperscript{136} All three are used in attempts to invalidate litigation finance agreements on the grounds that the financier was an outside party improperly involved in the case.\textsuperscript{137}

First, "maintenance is the 'assistance in prosecuting or defending a lawsuit given to a litigant by someone who has no bona fide interest in the case' or 'meddling in someone else's litigation.'"\textsuperscript{138} Next, champerty is maintenance with the added element of personal gain, where the party committing the offense does so in return for a share of the property.\textsuperscript{139} Finally, barratry is the "vexatious incitement to

\begin{itemize}
\item \textsuperscript{129} Id. at 239.
\item \textsuperscript{130} \textit{Lawsuit Fin.}, 683 N.W.2d at 240.
\item \textsuperscript{131} Cremandes, \textit{supra} note 90, at 174-76. \textit{See also} \textit{Echeverria v. Estate of Lindner}, 7 Misc. 3d 1019(A), at *1 (N.Y. Sup. Ct. 2005).
\item \textsuperscript{132} \textit{Echeverria}, 7 Misc. 3d 1019(A) at *1.
\item \textsuperscript{133} Id.
\item \textsuperscript{134} Id. at *8.
\item \textsuperscript{135} Id. at *12.
\item \textsuperscript{136} 15-83 \textit{CORBIN ON CONTRACTS} § 83.10 (2015) [hereinafter \textit{CORBIN}].
\item \textsuperscript{137} \textit{Id.} (citing \textit{Maintenance}, \textit{BLACK'S LAW DICTIONARY} (9th ed. 2009)).
\end{itemize}
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litigation, especially by soliciting potential legal clients. The Supreme Court explains the relationship between the three doctrines as follows: "maintenance is helping another prosecute a suit; champerty is maintaining a suit in return for a financial interest in the outcome; and barratry is a continuing practice of maintenance or champerty."

Interestingly, the doctrines arose in response to litigation financing arrangements in medieval England. In these arrangements, wealthier individuals would obtain interests in the legal claims of others, often in disputes over land titles. The financiers would receive a piece of the land in exchange for their investment. The risk involved in such disputes led wealthy parties to take all necessary steps to win, often resorting to unsavory practices including preventing "witnesses from appearing in court." The doctrines of maintenance, champerty, and barratry were meant to eradicate these practices.

In the United States, laws regarding these doctrines vary by state. There is some evidence that a third-party funding agreement may be voided entirely in a minority of states under one of these three doctrines. Some states, including Maryland and Mississippi, explicitly criminalize champertous agreements by statute. Overall, however, the trend across the country is toward limitations on the doctrine of champerty. For example, New York does not prohibit litigation finance arrangements as champertous so long as the case is already in existence and the litigant maintains control of the case.

Finally, some states that formerly recognized maintenance and

140. Cremandes, supra note 90, at 189 (citing Barratry, BLACK'S LAW DICTIONARY (9th ed. 2009)).
141. CORBIN, supra note 136, at § 83.10 (citing In re Primus, 436 U.S. 412, 424 n.15 (1978)).
142. Id.
143. Id.
144. Id.
145. Id.
146. CORBIN, supra note 136, at § 83.10.
147. Cremandes, supra note 90, at 189.
148. Id. A survey by Lisa B. Nieuwveld and Victoria Shannon shows that a litigation financing "agreement may be voided in nineteen states under the doctrines of maintenance, champerty, or public policy." Id. (citing LISA B. NIEUWVELD & VICTORIA SHANNON, THIRD-PARTY FUNDING IN INTERNATIONAL ARBITRATION 119 (2012)).
150. Cremandes, supra note 90, at 189 (citing Del Webb Cmtys., Inc. v. Partington, 652 F.3d 1145, 1156 (9th Cir. 2011)); see also AM. BAR ASSN'N COMM'N ON ETHICS 20/20, INFORMATIONAL REPORT TO THE HOUSE OF DELEGATES, WHITE PAPER ON ALTERNATIVE LITIGATION FINANCE 12 (2012).
champerty are eliminating these doctrines entirely. For example, in Saladini v. Righellis, the Massachusetts Supreme Judicial Court struck down all three doctrines.152 In Saladini, the plaintiff agreed to fund Righellis’s lawsuit in return for fifty percent of the recovery after attorney’s fees.153 The court held that the agreement was champertous but declined to uphold the doctrine, stating “we have long abandoned the view that litigation is suspect, and have recognized that agreements to purchase an interest in an action may actually foster resolution of a dispute.”154 South Carolina’s highest court soon followed suit, abolishing champerty as a defense in 2000, stating, “[w]e abolish champerty as a defense because we believe it no longer is required to prevent the evils traditionally associated with the doctrine as it developed in medieval times.”155

C. Alternative Public Policy Claims

A few courts have found alternative grounds for invalidating litigation financing agreements as violations of public policy. Such public policy claims are almost always included alongside claims of maintenance and champerty.156 A few states will analyze cases on a case-by-case basis, voiding agreements that perpetuate litigation or take advantage of one of the parties involved in the agreement to be purchased, while allowing those that are not overtly manipulative.

In Anglo-Dutch Petroleum International, Inc. v. Haskell, Anglo-Dutch Petroleum International, Inc. (Anglo-Dutch) filed a lawsuit against Halliburton and Ramco for misappropriation of trade secrets.157 In desperate straits, Anglo-Dutch entered into an agreement with a number of investors to fund the litigation and operate its business until it could recover a judgment.158 The company received $560,000 from investors.159 The trial court eventually entered judgment in favor of Anglo-Dutch in the amount

153. Id. at 1224-25.
154. Id. at 1226 (citing Joy v. Metcalf, 37 N.E. 671 (Mass. 1894)).
156. See Sneed v. Ford Motor Co., 735 So. 2d 306, 314 (Miss. 1999) (“The historical condemnation of champerty and maintenance is grounded in the estimable purpose of preventing the marketing of lawsuits . . . . ”); Johnson v. Wright, 682 N.W.2d 671, 678 (Minn. Ct. App. 2004) (citing Hackett v. Hammel, 241 N.W. 68, 69 (Minn. 1932) (“an agreement in which [a party] had no interest otherwise, and when he is in no way related to the party he aids, is champertous and void as against public policy”).
158. Id. at 90-91.
159. Id. at 91.
of $81 million. The company then refused to repay its investors, sending a letter disputing the validity of the funding agreement and requesting that they accept a reduced payment. Anglo-Dutch further asserted that refusal to accept the lower payment “put at risk Anglo-Dutch’s ability to resolve the lawsuit with Halliburton.” When no agreement was reached, the investors filed suit, alleging “breach of contract, fraud, breach of fiduciary duty, conspiracy, and conversion.” At trial, Anglo-Dutch contended that the agreements “prey on financially desperate plaintiffs, give [outside] parties control over litigation . . . and prolong litigation by inhibiting plaintiffs from settling lawsuits.” In addition, Anglo-Dutch asserted that the agreements were usurious and champertous.

The Court of Appeals dismissed all of Anglo-Dutch’s asserted defenses. The court found that the agreement was based on a real contingency and therefore could not be usurious. The court further noted that champertous agreements are not automatically void under Texas law. Finally, the court refused to void the agreement for being against public policy for giving outside parties undue influence over litigation. The court noted that Anglo-Dutch actively solicited the investments to cover its expenses and would not have been able to prosecute Halliburton without the funding. Further, the court found no evidence that the investors maintained control over any aspect of the Halliburton lawsuit. The court considered the following as possible methods of undue control: the ability to select counsel, “direct trial strategy, or participate in settlement discussions.” Finally, the court found no evidence that the agreement prolonged litigation.

160. Id.
161. Id.
162. Anglo-Dutch, 193 S.W.3d at 93.
163. Id. at 91.
164. Id. at 103.
165. Id. at 95.
166. Id. at 103.
167. Anglo-Dutch, 193 S.W.3d at 105.
168. Id. at 98.
169. Id. at 104.
170. Id. at 105.
171. Id. at 104.
172. Anglo-Dutch, 193 S.W.3d at 104.
173. Id.
174. Id.
D. Gambling

One final claim that has been advanced as a defense to a litigation financing arrangement is that the agreement itself violates illegal gambling statutes. While courts have discussed the possibility of such agreements violating gambling laws, only Alabama has invalidated litigation finance contract for violating such a statute. In Wilson v. Harris, Annie Harris sued Sears, Roebuck & Company, and other defendants, for wrongful death. The case was pending on appeal for two years at great cost to Harris. Wilson, a close friend, agreed to advance Harris money in exchange for a portion of the recovery. The Court of Appeals held the agreement between the two parties to be in violation of Alabama’s gambling laws, which prohibit “all contracts founded in whole or part on a gambling consideration.” No other court has followed the ruling in Wilson, and several courts have taken the opposite position. In Odell v. Legal Bucks, the court determined that the litigation finance agreement did not fit into the precise definition for what constitutes a “wager” or “bet” under the laws of North Carolina.

IV. THE CASE AGAINST ALLOWING CROWDFUNDED LITIGATION FINANCING

While there are many pitfalls and risks associated with traditional third party litigation financing, there are clear signs that the industry is becoming more accepted in states where it is still permitted. Some states, such as Maine, Nebraska, and Ohio, have even launched efforts to regulate the industry.
In 2007, Maine amended its Consumer Credit Code to include regulations for the litigation financing industry. These regulations, the Maine Consumer Credit Code Legal Funding Practices (Funding Practices), require litigation financing providers to register with a state administrator, a process involving a demonstration of financial responsibility. The Funding Practices require financing agreement contracts to be "clear and coherent" and provide for full disclosure, including the calculation of the annual percentage rate. Further, the contracts must inform the borrower that the company providing the funding has no right to make any decisions in the borrower's case.

In 2008, Ohio enacted O.R.C. § 1349.55, which sets forth similar disclosure requirements, including the itemization of all one-time fees, the annual percentage rate, and a notification that the financier has no right to dictate the underlying case. Notably missing from the Ohio regulations, however, is the registration requirement included in the Maine statute.

In 2010, Nebraska enacted its Nonrecourse Civil Litigation Act (Act). Like the Maine statute, the Act requires registration. The Act allows the Secretary of State to refuse registration to any litigation finance firm that it deems unfit or financially irresponsible. In addition, the Act requires the Secretary of State to gather information from registered firms, including the number of litigation contributions, the amount of such contributions, and the amount charged to borrowers.

These regulations are an excellent start toward fully regulating the litigation financing industry. However, they do not address some of the major issues posed in crowdfunded litigation financing, as they only regulate relations between the finance firm and the plaintiff. No regulation currently exists in the United States to protect defendants from the potentially disastrous effects of litigation financing: an increased risk of frivolous litigation, as well as trial by media.
A. Risk of Frivolous Litigation

As discussed in Part II, crowdfunding websites take advantage of the proliferation of the Internet to reach a mass audience. Once uploaded onto a crowdfunding website, anyone with a computer, phone, or tablet can contribute to a project. No single user need to contribute more than a few dollars for the project to meet its goals. Using this method, crowdfunded projects are capable of raising a substantial amount of funding in a startlingly short period of time. For example, the list of the most funded projects on Kickstarter since inception in 2009 includes almost 100 projects that successfully raised over $1 million through crowdfunding in less than sixty days.\(^{194}\) Of this number, at least eight projects were able to raise $1 million in less than a single day, one raising $1 million in under thirty minutes, entirely through crowdfunding.\(^{195}\)

This phenomenon, with respect to litigation financing, would open the door to frivolous litigation. Traditional litigation funding firms must carefully vet each case before they make any investment decisions.\(^{196}\) A single firm will often lend a considerable amount of money to a plaintiff. Should that plaintiff lose, the firm recovers none of its investment.\(^{197}\) A litigation financing agreement that seeks to eliminate this contingency by requiring some form of payment, even if the plaintiff loses, risks the invalidation of the entire agreement under usury laws.\(^{198}\) This leaves traditional litigation finance firms with an all-or-nothing proposition that forces them to weed out any potential frivolous lawsuits; a firm that takes on too many risky cases will not be able to turn a profit.

A crowdfunded litigation financing arrangement would not be subject to the same limitation. As crowdfunding generally relies on relatively small monetary commitments by a large number of individuals, relatively expensive claims can be completely funded without any single individual risking a substantial sum of money.\(^{199}\) While in the past, an individual or firm wishing to enter the litigation


\(^{196}\) See supra Part II.

\(^{197}\) Id.

\(^{198}\) See supra Part III.A.

\(^{199}\) See supra Part II.
financing industry would need to invest a large amount of money in small number of cases, crowdfunding makes investing in individual cases as easy as purchasing stock. An investor could limit her risk by investing miniscule sums in a wide variety of cases. One could easily imagine certain investors building a portfolio that includes stocks, bonds, and legal disputes. While hedge funds and firms already invest in lawsuits in the litigation finance industry,200 crowdfunding further reduces their risk by limiting their involvement in any one suit and allowing them to spread out their investments.

Lowering the risk of losing an individual or firm's entire investment over the outcome of a single case also means that investors can be less selective when choosing their cases. Where, traditionally, firms could choose only those few cases that had the strongest legal merits, the sizeable reduction of risk means that firms that utilize crowdfunded litigation financing may invest in a larger volume of cases that have a smaller likelihood of success. This leaves room for additional investments, potentially increasing the overall size of the litigation financing market.

Because reducing the risk and costs associated with lending makes the market more accessible to more investors, crowdfunded litigation financing also allows for the reduction in out-of-pocket costs for a larger number of prospective plaintiffs. Many of these plaintiffs will be those that have cases that would have been seen as too risky for traditional firms to invest in. As the litigation financing market grows and investors become more willing to invest in less meritorious cases for the chance of a high payout, the number of plaintiffs receiving funding will increase as well.

This reduced risk for plaintiffs means that more parties will be less willing to settle. To explain this, one must understand the methods used by plaintiffs in deciding whether to litigate their case. In determining whether to go forward with a claim, one calculation is to take the amount plaintiffs are likely to win if their claim is successful and multiply it by the estimated chance of success.201 This number, subtracted by the cost of litigation, is used to determine both how much a case is worth and whether the plaintiff should accept a given settlement offer from the defendant.202 As cost and likelihood of


202. Id. For example, if a plaintiff could potentially win $1 million in damages, but his attorney estimates that he is only twenty-five percent likely to succeed and would cost $100,000 to litigate after consulting experts, potential appeals, etc., the claim would be worth $150,000. In this case, plaintiff
success are two of the most important factors in deciding whether plaintiffs go forward with their claims, this will mean more cases will go to court, as plaintiffs hold out for a favorable verdict or a higher settlement. In addition, the reduced risk for plaintiffs and larger number of investors also means that more plaintiffs will be able to bring their claims to court in the first place, resulting in more lawsuits.

Finally, the business model typically used by crowdfunding websites itself increases the risk for frivolous litigation. Typically, crowdfunding platforms receive a commission in exchange for the right to post a project on their website. LexShares and Funded Justice serve as examples of this, as both websites profit from their clients’ cases. Both businesses receive a commission from each project, regardless of whether the litigation is successful, meaning they may well earn more money by listing more projects.

B. Trial by Media

In addition to the greatly-increased risk of frivolous litigation, there is also the risk that crowdfunded litigation financing will lead to a greater danger of trial by media. Both LexShares and Funded Justice are marketed as a boon to plaintiffs who have meritorious cases but lack the necessary funds to hire a knowledgeable and dedicated attorney. The “About Us” page on the Funded Justice website invokes the plight of the middle class, proclaiming that “[f]or too long, the rich have always had access to the best legal minds that money could buy, and people that were indigent have always had access to legal aid clinics based on their income.” It continues, saying “the vast majority of Middle America . . . would find it difficult to come up with thousands of dollars on short notice to help a family friend [get legal services].” LexShares’ website similarly

would be likely to accept a settlement offer of $250,000 if he had to foot the entire bill. However, if the plaintiff only expected to pay half that amount, having received the other half from investors, he would be more willing to risk litigation, especially knowing that he would have to pay a substantial portion of the settlement back to his investors.


204. See supra Part II.

205. Id.


207. Id.
states, "[I]literation finance through LexShares equalizes access to justice." The potentially large online audience and the altruistic presentation of each case creates a very real danger of trial by media, as information found on these websites can be spread through social networks.

In addition to its capacity to reward funders and provide them with equity in new businesses, crowdfunding has also long been used to advance social causes, relying on social media as well as traditional news outlets to rapidly disseminate popular causes. Social media outlets like Facebook and Twitter have themselves been popular forums for seeking social justice. There is no reason to expect that the same will not hold true for the crowdfunding of litigation financing. News of poor plaintiffs seeking justice can quickly spread over to these outlets and others, soliciting large volumes of individuals to donate or invest in a cause they believe to be worthy of their sponsorship. Popular social media movements, when entrenched, can become difficult to counter.

As the defendants in litigation finance claims are generally corporations (with suitably deep pockets), the media exposure that crowdsourcing could bring to a case that might otherwise be ignored by traditional media outlets could be disastrous. When facing litigation, corporate defendants are concerned not only about the outcome of the case, but also the impact that the case may have on the company's public image. Large and publically traded companies face particularly large threats from high-profile lawsuits. In cases where the public closely follows litigation, bad publicity could have a significant impact on the goodwill of customers, as well as significantly damage a company's stock price. This danger will only be magnified as crowdfunding of litigation financing becomes...
In addition to worrying about the impact that individuals may have on good will or stock prices, litigation financing introduces a third danger. Individuals may contribute funds to a lawsuit against a company simply because they oppose the company’s business practices. This is not particularly difficult to imagine, especially in more politically-controversial industries. Another troubling possibility is that of a business investing in litigation against a rival company, hoping that the ensuing court battle and media coverage gives them a competitive advantage. As individual contributions are only a small portion of the total funds, and financers are generally not considered, as they have no legal control over litigation, there is likely very little recourse in either of these scenarios.

There are several real-world examples of impromptu social media campaigns over seemingly minor issues that damaged public goodwill in a corporation. In 2008, after a United Airlines flight, professional musician Dave Carroll discovered that his guitar was broken.212 Earlier, Carroll and several other passengers had observed baggage handlers mistreating the guitar and had warned a flight attendant, who told Carroll that nothing could be done.213 Carroll spent several months attempting to resolve the dispute, only to have his claim denied because he had not filed a formal complaint within twenty-four hours of the incident.214

Frustrated by the experience, Carroll decided to turn to social media, producing a song called “United Breaks Guitars.”215 The song quickly spread and within five days the video had been viewed 1.7 million times on the video website YouTube.216 Mainstream news outlets like CNN and the CBS morning show began calling United for interviews by the end of the week, and United was forced to quickly shift into damage control.217 The company admitted wrongdoing, donated $3000 to a music school as a gesture of goodwill, and implemented changes in its customer-service practices in response to the incident.218 All told, the song had a very negative effect on United’s brand equity, and may have even damaged the

213. Id. at 53-54.
214. Id. at 54.
215. Id. at 55.
216. Id. As of Mar. 28, 2015, the video has over 14 million views. Sons of Maxwell, United Breaks Guitars, YOUTUBE (July 6, 2009), https://www.youtube.com/watch?v=5YGc4zOqozo.
217. Morales, supra note 212, at 55.
218. Id. at 56.
company’s stock price.219

A similar incident occurred in 2005. Jeff Jarvis purchased a Dell laptop along with an expensive four-year, in-home warranty.220 The laptop suffered from several malfunctions, and Jarvis was informed that he would have to send his laptop in for repair despite his in-home warranty.221 Jarvis complained about his experience on his blog, “The Buzz Machine.”222 The computer continued to malfunction, and Jarvis continued his campaign against the company.223 Hundreds more consumers joined in, all complaining about Dell’s customer service.224 Eventually, mainstream media took notice, with both the New York Times and Business Week addressing the topic.225 In the end, Jarvis’ “Dell Hell” campaign had a negative impact on the reputation and sales of the company.226

These two situations demonstrate the power for relatively minor incidents to develop into full-fledged negative public relations campaigns over social media. If a single broken guitar or faulty laptop could hurt a company’s public image, imagine the damage that a crowd-funded class-action lawsuit could do. If crowd-funded litigation finance campaigns manage to reach the popularity level of the “United Breaks Guitars” video or one of the nearly 100 Kickstarter campaigns to reach over $1 million in less than two months, companies could quickly find themselves lost in litigation over issues that might have been settled or dropped altogether.

V. CONCLUSION

For better or worse, traditional litigation financing has become an accepted reality in the majority of the United States. If well-regulated by the states and federal government, some forms of litigation financing arrangements can be mutually beneficial for plaintiffs and their investors. After all, litigation finance firms provide plaintiffs with desperately-needed funding in their cases while giving those with the money and legal acumen to carefully

219. Within four days of the song’s release, United’s stock price dropped ten percent, costing shareholders $180 million. Ravi Sawhney, Broken Guitar has United Playing the Blues to the Tune of $180 Million, FAST COMPANY (July 30, 2009), http://www.fastcompany.com/1320152/broken-guitar-has-united-playing-blues-tune-180-million.
220. Morales, supra note 212, at 50.
221. Id.
222. Id.
223. Id. at 51.
224. Id.
225. Morales, supra note 212, at 51-52.
226. Id. at 50.
consider the merits of each case another avenue of investment. And because of the considerable risk involved, investors will always be careful to scrutinize any potential investment opportunity.

Introducing crowdfunding to the litigation financing world, however, is a dangerous misstep. By diluting the risk to any individual investor or firm, crowdfunding makes it easier for those with little legal knowledge to invest in any case they feel strongly about, with little risk involved. This will, in turn, lead to ill-advised investment decisions in plaintiffs with less than meritorious claims, and may reduce a plaintiffs' willingness to settle. Finally, as plaintiffs are offered opportunities to receive funding from investors through the Internet, they will inevitably describe their cases in the most positive light possible. Investors and crowdfunding platforms that also seek to profit from these claims will further encourage this positive portrayal. Defendants, big or small, will have no comparable public forum to defend themselves against potential damage to their reputations. If allowed to grow unchecked, crowdfunded litigation financing could have a major impact within the legal system.