KANSAS SENATE JUDICIARY COMMITTEE
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ON BEHALF OF THE U.S. CHAMBER OF COMMERCE
INSTITUTE FOR LEGAL REFORM

SENATE BILL 74 – PROPONENT TESTIMONY

Thank you for the opportunity to testify in support of S.B. 74, lawsuit funding disclosure legislation, on behalf of the U.S. Chamber of Commerce Institute for Legal Reform ("ILR"). The U.S. Chamber is the world's largest business organization representing companies of all sizes across every sector of the economy. Many Kansas businesses are members of the U.S. Chamber.

As part of its core mission, ILR has been studying the effects of third-party litigation funding ("TPLF") for more than a decade. The ILR has sponsored a number of nonpartisan symposia and conferences, as well as the publication of research reports on the effects of TPLF in the United States. In addition, ILR has engaged in public advocacy in state legislatures, the U.S. Congress, and the judiciary. ILR welcomes the opportunity to explain the dangers TPLF poses to Kansas's civil justice system and why S.B. 74 should be enacted to mitigate those problems.

TPLF

Investor groups are pouring unprecedented sums of money into financing litigation in the United States. Third-party litigation funders front money to plaintiffs' law firms in exchange for an agreed-upon cut of any settlement or money judgment.

As Professor Donald Kochan of the Antonin Scalia Law School at George Mason University explained in a recent *Wall Street Journal* editorial, "Third-party litigation funding turns the American justice system into a financial playground by transforming lawsuits into investment vehicles." (Donald Kochan, Editorial, *Keep Foreign Cash Out of U.S. Courts*, Wall St. J., Nov. 25, 2022, at A13). Investors are attracted by potentially hefty returns that are not tied to economic or market conditions.

Commercial litigation funding began in Australia, made its way to the UK and Europe, and arrived in the U.S. about a decade ago. The practice has taken off in recent years with the loosening of longstanding common law doctrines on maintenance, champerty and barratry that prohibited the outside financing of litigation.

According to a December 2022 report by the U.S. Government Accountability Office (GAO), "the best available estimates of the size of the U.S. commercial TPLF market...identified 47 active commercial litigation funders, and reported that they had a total of $12.4 billion in assets under management and had committed $2.8 billion to new litigation financing agreements in 2021." (United States Government Accountability Office, GAO-23-105210, *Third-Party Litigation Financing: Market Characteristics, Data, and Trends* (Dec. 2022)).

Along with the growth of TPLF in general, there is a trend for larger investment firms to move away from financing individual cases in favor of investments in pools of cases.

Litigation funders view lawsuits as assets, just like any other receivables. One of the TPLF industry's largest companies, Burford Capital LLC, explained in an Annual Report: "It may seem strange to think of litigation in that way, but if one strips away the drama and the collateral dynamics associated with the litigation process, a litigation claim is nothing more than an effort to get money to change hands." Burford is a publicly traded global finance firm focused on litigation funding.

Proponents of TPLF claim that the practice levels the field between large, well-financed litigants who are used to fighting in court and individuals or small to mid-sized companies who are often inexperienced at fighting legal battles and may find themselves outgunned.

ILR and other business and civil justice organizations believe that TPLF leads to the filing of speculative lawsuits, because litigation funders absorb some of the risk in litigation and can spread it across a portfolio of cases and among investors.

Additionally, a funder's presence can unreasonably prolong cases and frustrate settlements. The presence of a third-party litigation funder can change what is essentially a two-party negotiation into a multi-party settlement with a "behind the table" constituent.

TPLF practices also raise serious ethical issues, such as a threat to a lawyer's ability to exercise independent judgment in cases where the funder has authority to make key litigation decisions.

Presently, in most states, TPLF arrangements generally do need not be disclosed—and therefore largely remain hidden from public scrutiny. Further, unlike other financial products, TPLF is largely unregulated. The practice operates with little to no transparency, making it difficult for judges and parties to know who has an interest in the outcome of the litigation.

ILR believes that courts should know if their efforts to settle cases may be complicated by an entity that is not in the room.

Courts also might be more open to defendant requests for cost-shifting in cases involving burdensome discovery if they are aware that there is not a wide disparity in each side's ability to pay. A multi-million dollar hedge fund that is making a business decision to invest in a case for profit should not be entitled to the same producer-pays free ride as an impecunious citizen.

Where sanctions are appropriate for misconduct, courts need to know about the presence of a third-party in the litigation to determine how to impose sanctions or other costs.

Further, disclosure of funders can help courts police litigation that is filed or prolonged for improper purposes. A few high-profile cases have highlighted the potential for third party funders to sponsor litigation for ulterior purposes such as personal revenge or improper business tactics.

A newer concern is the potential for foreign financiers to exploit the lack of transparency with regard to TPLF to "weaponize the courts for strategic goals." According to Prof. Kochan, foreign adversaries such as China or Russian may fund lawsuits in the United States to "weaken critical industries" or "obtain confidential materials through the discovery process." The issues are discussed in a 2022 ILR report, *A New Threat: The National Security Risk of Third Party Litigation Funding*.

In December 2022, Kansas Attorney General Derek Schmidt joined over a dozen other state attorneys general in writing the U.S. Department of Justice to ask U.S. Attorney General Merrick Garland and other top officials about steps being taken to protect the country against potential national security threats posed by TPLF. The state attorneys general wrote: "It is impossible to know the extent that foreign adversaries are spending on American litigation through TPLF, which leads to significant concern that TPLF is being used to harm our States and threaten our country's economic and national security." GAO acknowledged in its 2022 report that in addition to "sophisticated private entities, such as endowments and pension funds," investors in at least two funders "also included sovereign wealth funds, which are government-controlled funds that seek to invest in other countries…."

TPLF is attracting increasing public attention. In December 2022, CBS News show *60 Minutes* did a segment on TPLF. The CEO of Burford—"which has $5 billion invested in multiple lawsuits"—said his company picks cases very carefully, telling Lesley Stahl, "We are right about 90% of the time…." "On an average basis," he added, "we'll largely double our money." (60 Minutes, *Litigation*

Funding: A Multibillion-dollar Industry for Investments in Lawsuits With Little Oversight (Dec. 18, 2022), https://www.cbsnews.com/news/litigation-funding-60-minutes-2022-12-18/).

Professor Maya Steinitz of the University of Iowa College of Law told *60 Minutes* the public should care about TPLF because litigation funders "are reshaping every aspect of the litigation process—which cases get brought, how long they are pursued, when are they settled. But all of this is happening without transparency. So we have one of the three branches of government, the judiciary, that's really being quietly transformed."

S.B. 74

S.B. 74 would shine much needed light on TPLF. The bill requires disclosure of a litigation financing agreement in which a third party not before the court fronts funds to a party in exchange for obtaining a contractual right to a portion of any litigation proceeds. To discourage frivolous claims, the bill will hold litigation funders and plaintiffs jointly liable for costs and sanctions. Further, a party in a third-party funded action must reasonably compensate a nonparty for the cost of responding to a subpoena to produce information, permit the inspection of its premises, or appear at a deposition.

The bill promotes transparency in light of the proliferation of TPLF agreements that may conceal the true nature of the interests underlying a litigation and may enable a third party to exert influence on a party or attorney. Because such an agreement carries a potential to significantly impact the just, speedy, and inexpensive determination of an action, disclosure should be required.

In 2018, Wisconsin became the first state to require a party's initial disclosure of any third party litigation financing agreement. *See* Wis. Code § 804.01(2)(bg). In 2019, West Virginia adopted a similar disclosure requirement for consumer lending lawsuits. *See* W. Va. Code Ann. § 46A-6N-6.

Adoption of S.B. 74 puts Kansas in the legal mainstream and is consistent with the clear trend toward transparency. *See* U.S. Chamber of Commerce Institute for Legal Reform, *Selling More Lawsuits Buying More Trouble* (Jan. 2020); David H. Levitt with Francis H. Brown III, *Third Party Litigation Funding: Civil Justice and the Need for Transparency*, DRI Ctr. for L. & Pub. Pol'y, Third Party Litigation Funding Working Group, at 31-32 (2018).

For these reasons, ILR supports enactment of S.B. 74.